Dr. Neha Agrawal,
Dr. Nikita Singhal

INDIAN FINANCIAL SYSTEM

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CHAPTER 1

FEATURES OF INDIAN FINANCIAL SYSTEM

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ABSTRACT:
The Indian financial system is a complex and dynamic structure that plays a pivotal role in driving the country's economic growth and development.

This paper aims to explore the key features of the Indian financial system and their significance in shaping the nation's financial landscape. The study delves into various components, such as banking, capital markets, insurance, and regulatory institutions, to provide a comprehensive understanding of the system's functioning.

Through an analysis of historical developments and recent trends, this research sheds light on the strengths, challenges, and potential areas of improvement within the Indian financial system. The findings emphasize the critical role of a well-functioning financial system in fostering economic stability, promoting investment, and channeling financial resources to support sustainable growth. However, the study also highlights the need for continual reforms and policy interventions to address existing bottlenecks and ensure a robust and inclusive financial ecosystem for all stakeholders.

KEYWORDS:

Asset Management, Banking, Central Board, Corporation, Commodity Derivatives.

INTRODUCTION

Lenders and borrowers are able to trade money because to the financial system. In the areas of insurance, banking, capital markets, and different service industries, India's financial system is governed by independent authorities. The ability of a financial system to mobilize excess money and use them efficiently for productive purposes may thus be considered to contribute significantly to a nation's economic development[1], [2].

Indian financial system characteristics:

1. It is essential to a nation's economic progress.
2. It promotes investing as well as saving.
3. It connects investors and savers.
4. It promotes the production of capital.
5. It aids in risk allocation.
6. It makes financial market growth easier.

The Indian Financial System is made up of the four main principal elements:

1. Institutions of finance
1. 2.Financial Markets
2. Financial Assets, Securities, and Instruments
3. The financial sector.

Institutions of finance

By bringing investors and borrowers together, financial institutions act as middlemen and help the financial system run smoothly. They mobilize the extra unit savings and invest them

in profitable ventures that promise a higher rate of return. Financial institutions also provide services to organizations looking for guidance on a range of topics, from restructuring to diversification strategies. They provide a wide variety of services to organizations looking to raise money on the open market or elsewhere[3], [4].

Financial institutions are also known as financial intermediates because they serve as a bridge between savers and borrowers by collecting funds from savers and lending those funds to the latter. Due to the fact that they receive deposits from a variety of consumers, they also serve as middlemen. Mutual funds act as financial intermediaries by amassing deposits and lending them to borrowers, much as shrewd investment organizations like ICCIC.

Banking Establishments

The Central Bank has responsibility over the banking sector in India. The country's monetary and financial systems are organized, managed, monitored, regulated, and developed by the RBI in its capacity as the apex institution. The Banking Regulation Act of 1949 is the primary piece of law that controls commercial banks in India[5], [6].

Two main categories may be used to categorize Indian financial institutions:

1. Organizing Sector
2. Unorganized Sector

Business banks:

Commercial banks might be either scheduled or unscheduled. Only one bank is not currently planned. Schedule banks comprise all other banks. There are 27 commercial banks, including private, state, and international institutions. With the exception of State Bank of India, all significant banks operated in the private sector until 1969. When 14 large commercial banks with a deposit base of $50 billion or more were nationalized in July 1969, it was a significant step toward the development of public sector banking. Another 6 banks were nationalized later in 1980, bringing the total number of nationalized banks to twenty[7], [8].

Banking cooperatives:

Co-operative banking is a significant component of Indian banking's organized sector. A collection of societies recognized under state laws governing cooperative societies serve as the segment's representative. Cooperative societies might really be credit or non-credit organizations. The Indian economy is home to several varieties of cooperative credit organizations. Two major categories may be used to group these institutions: Rural credit societies, where agriculture is the main industry, and urban credit societies, where non-agricultural is the main industry. There are many cooperative credit institutions for agricultural purposes to accommodate various demands.

Rural regional banks:

To advance the rural economy, regional rural banks were established by the state government and sponsored commercial banks. Small farmers and small business owners in rural regions may get financing from regional rural banks. The regional rural banks were established with the intention of giving weaker people access to loans. They make up a significant portion of India's rural banking infrastructure. At the end of June 2002, there were 196 RRBs, compared to 107 in 1981 and 6 in 1975.Banks from abroad: Indian banks are foreign from the days of the British Empire. Foreign banks are defined as banks with primary headquarters in one country and branches in other nations. Numerous international banks are entering India as a result of the liberalisation that occurred in 1993. Citi Bank is a foreign bank. [9], [10].

2.Unorganized Sector

Indigenous bankers and money lenders operate in the unorganized banking industry.

1. **Native bankers**

Private companies or individuals operating as banks are known as indigenous bankers. As such, they accept deposits and disburse loans. They are financial mediators, much like bankers. They should be reputable professionals who specialize in lending money rather than banking or lending money. The domestic banks trade in commercial paper known as "hundis."

2. **Lenders of money:**

Lenders of money rely only on their own cash. Rural or urban, professional or unprofessional, money lenders are possible. They consist mostly of farmers, businesspeople, and traders. Their business practices are totally ungoverned. They impose exceedingly high interest rates.

DISCUSSION

Non – Banking Institutions

The Organised non - banking financial institutions include:

1. Development Finance Institutions.

the national level organizations like IDBT, ICICI, IFCI, IIBI, and IRDC. State-level institutions include State Finance Corporations and State Industrial Development Corporations. NABARD, LDBS, and other institutions that finance agricultural development. Development banks engage in initiatives to promote economic development in addition to providing medium- and long-term financing to the business and industrial sector.

2. Financial institutions.

These financial organizations include those that elicit savings from the general people via a variety of programs and invest those monies in corporate and governmental assets. These include mutual funds, LIC, GIC, and LTT.

In distinct chapters of this book, the non-banking financial institutions in the organized sector have been covered in great depth.Organizationally Disorganized Non-Banking Financial Institutions Numerous non-banking financial enterprises offering a wide variety of financial services are included in the unorganized non-banking financial organizations.

The 300 consumer finance firms, leasing companies, home finance companies, factoring companies, credit rating agencies, merchant banking companies, etc. are among them. NBFCs supply loanable money and raise public capital.

Financial Sector

The financial system of an economy operates via financial markets and institutions. The institutional arrangements for trading in financial assets and credit instruments of various forms, such as money, checks, bank deposits, bills, bonds, etc., are referred to as financial markets.

The following are the purposes of financial markets:

1. To promote the development and distribution of credit and liquidity

2. To act as middlemen in the mobilization of savings.
3. To aid in the expansion of the economy in a balanced manner.
4. To make money easier to access.

Financial Market

Financial assets with a protracted or undetermined maturity are traded on the capital market. It often deals with long-term securities having maturities longer than a year. Three categories further split the capital market:

Market For Industrial Securities

Long-term loans and the market for government securities

The market for industrial securities

It is a market for industrial securities, specifically:

1. Equity shares or ordinary shares,
2. Preference shares, and
3. Debentures or bonds, as the name already suggests.

It is a market where business concerns may issue the proper instruments to obtain money or debt. It may be broken into two further categories. As follows:

1. new issue market or the primary market
2. Stock exchange or secondary market

Primary Market

A primary market is one where fresh financial claims or issues are traded. As a result, it is also known as New Issue market. Securities that are originally released to the public are dealt with in the primary market. Borrowers trade brand-new financial instruments for long-term money in the main market. Therefore, the primary market aids in capital generation. In a primary market, a corporation may raise money in one of three methods. As follows:

1. Public concern
2. Rights concern
3. Independent placement

The public sale of securities is the most typical way for new businesses to get financing. It's known as a public problem. Securities are initially issued on a pre-emptive basis to the current shareholders when an established firm needs to raise more money. It's known as a rights problem. Selling stocks privately to a select group of investors is done via a private placement.

Secondary Market

A secondary market is a market where securities are sold to other investors. In other words, shares traded in this market have previously been through the fresh issue market. These securities are often listed on the Stock Exchange, which offers a consistent and regular market for buying and selling stocks. All stock exchanges recognized by the Indian government are included in this market. The Securities Contracts Act of 1956 governs the stock markets in India.

The primary stock exchange in India, the Bombay Stock Exchange, sets the standard for all other stock exchanges.

Market for Government Securities

Other names for it are Gilt-Edged Securities Market.

Government securities are traded on this market. Both short-term and long-term government securities are widely available in India. This market is where long-term securities are exchanged, while the money market is where short-term securities are traded. Improvement Trusts, State Electricity Boards, All India and State level financial institutions, public sector firms, and securities issued by the Central Government, State Governments, Semi Government bodies like City Corporations, Port Trusts, etc. are all traded in this market.

Market for Long-Term Loans

By offering long-term loans to corporate clients, development banks and commercial banks contribute significantly to this sector.The market for long-term loans may also be divided into:

Term Loans Industry

The government of India has established many industrial finance organizations at the national and regional levels in order to provide long- and medium-term loans to corporate clients both directly and indirectly. In India, these development banks predominate in terms of financing for industry. This category includes organizations like IDBI, IFCI, ICICI, and other financial businesses.

Mortgage Industry

A mortgage loan is a loan taken out in exchange for real estate or other immovable property as security. Mortgage refers to the sale of a particular immovable property's interest to fund a debt. This mortgage might be a legal or equimortgage.

Cash Market

The money market is a market where financial assets and securities with maturities of up to one year are traded. It is a market for just short-term investments, in other words. Four categories may be used to separate the money market.

Telephone Money Market

A market for loans with very short terms, such as one day to fourteen days, is the call money market. It is thus quite liquid. The borrower or lender may choose to seek repayment of the debts at any time.

Call money markets are found in India's main industrial cities such as Bombay, Calcutta, Madras, Delhi, Ahmedabad, etc. since they are connected to stock exchanges. This market's unique characteristic is the variation in interest rates from day to day, and even from hour to hour and center to center. It is very sensitive to changes in the supply and demand for call loans.

Market for Commercial Bills

It serves as a market for bills of exchange resulting from legitimate business dealings. The seller may draw a bill of exchange on the buyer in a credit sale scenario. Such a bill is accepted with the buyer's promise to pay at a later time set out in the bill. The vendor is not required to wait until the bill's due date. Instead, he might discount the charge to get payment right away.

Market for Treasury Bills

It is a market for Treasury Bills with ‘short-term' maturities. A treasury bill is a finance bill or promissory note that the government has issued. Due to the government guaranteeing its repayment, it is quite liquid. It is a crucial tool for the government's short-term borrowing. Treasury notes come in two varieties: normal or ordinary and ad hoc treasury bills, sometimes referred to as "ad-hocs." In order to raise money for the Central Government to satisfy its immediate financial requirements, ordinary treasury bills are issued to the general public, banks, and other financial institutions. Ad hoc treasury banknotes are only issued in the RBI's favor. They are not offered for sale at a bid or an auction. Only the RBI is able to buy them. Ad-hocs are not traded in India, although their owners may return them to the RBI.

Market for Short-Term Loans

In this industry, short-term loans are provided to business clients to help them with their working capital needs. Commercial banks are quite important in this sector. Commercial banks provide overdrafts and cash credit as short-term borrowing options. Businesspeople often get over draft privileges, while industrialists receive monetary credits.

The current account itself is used to provide an overdraft, which is just a short-term accommodation. However, cash credit is authorized in a separate account and is valid for a year.

Monetary Instruments

Documents that reflect financial claims on assets are referred to as financial instruments. Financial assets, as was previously mentioned, are claims to the return of a certain amount of money at the conclusion of a specific term, together with interest or dividend. Examples include Treasury Bills, Promissory Notes, and Bills of Exchange.

Basic Securities

These securities were issued straight from the ultimate savers to the final investors. For instance, publicly issued shares and bonds.

Additional Securities

These are securities provided to the end savers by certain middlemen known as financial intermediaries.

For instance, the Unit Trust of India and mutual funds sell units of securities to the public, and the money that is pooled is then invested in businesses. Once again, these securities may be grouped according to duration as follows:

1. Short-term investments
2. Long-term investments

Long-term investments.

Securities having a one-year maturity or less are referred to as short-term securities. For instance, a Treasury bill or a bill of exchange. Securities classified as medium-term have maturities between one and five years.

Long-term securities are those having a maturity length of more than five years, such as debentures maturing in less than five years. For instance, government bonds with a 10-year maturity.

Monetary Services

The caliber and range of financial services offered by financial intermediaries heavily influence the effectiveness of the developing financial system. Financial services are described as "activities, advantages, and pleasures associated with the sale of money, that provide users and customers with value that is financially related." Banks, financial institutions, and non-banking financial enterprises make up the three major segments of the financial services sector.

Financial Services Types

Two main categories may be used to describe the financial services offered by different financial institutions, commercial banks, and merchant bankers.

1. Fund- or asset-based services.
2. Services with a fee or advice.

Services based on assets or funds

Briefly described are the asset and fund-based services offered by banking and non-banking financial entities.

1. Leasing or financing of equipment

Without purchasing and owning the assets, leasing enables a company to utilize and manage such assets. It is a kind of asset rental. However, the company is not required to own the asset in order to invest. Basically, it wants to utilize the asset, which is its interest. As a result, instead of purchasing the asset, the company may think about leasing it.

When comparing the costs of leasing versus purchasing, the cost of financing the asset with debt and equity, as opposed to leasing, should be taken into account. Since paying lease rents is analogous to paying interest on debt, and financing a lease is equal to taking on debt.

2. Hire Purchase and Credit for Consumers

Hire purchase refers to a transaction in which goods are bought and sold on the condition that payment will be made in installments, possession of the goods is given to the buyer right away, the property ownership in the goods remains with the vendor until the last installment is paid, the seller has the right to reclaim the goods in the event that any installment is not paid on time, and each installment is treated as hire fees until the last installment is paid. Consumer credit refers to any asset-based lending options made available to people to assist them in purchasing durable consumer items.

In a transaction involving consumer credit, the person, consumer, or buyer pays a portion of the cash purchase price at the time the item is delivered and pays the remaining amount with interest over a certain period of time.

3. Venture Capital

In the Indian capital industry, venture capital financing is one of the newest players. Because more technocrat entrepreneurs are emerging in our nation but lack the funds to take risks, there is a huge market for venture capital firms.

These venture capital firms provide entrepreneurs the risk capital they need to fulfill the promoter's contribution requirements set out by the lending institutions. These VCFS take an active interest in directing the aided enterprises in addition to providing cash.

4. Insurance Services

Insurance is a contract wherein the insurer, i.e., insurance company, agrees or undertakes, in exchange for a monetary payment, to compensate the beneficiaries in the event of a specified event, such as an accident or death, or to make good the loss suffered by the insured against a specified risk, such as fire. The phrase "policy" refers to the written agreement, in black and white, between the insurer and the insured. The object of insurance is the property that is insured. Insurable interest is the interest that the insured has in the object of the insurance. Insurance services are categorized into life general depending on the topic.

5. Factoring

As a fund-based financial solution, factoring offers resources to finance receivables and makes it easier to collect them. Another way to get short-term financing is via the provision of account receivable credit by commercial banks and factoring. A commercial bank may provide financing by giving discounts on its clients' bills or invoices. As a result, a business receives prompt payment for credit sales. A financial organization known as a "factor" provides administration and financing services for debts resulting from credit sales.

CONCLUSION

In conclusion, the distinctive characteristics of the Indian financial system have established a solid base for economic expansion and success. India can position itself as a global financial powerhouse, promoting sustainable development, and improving the lives of its population by capitalizing on these assets and resolving the mentioned difficulties. A durable, effective, and inclusive financial system for the country's future will be shaped through continued cooperation between the public and private sectors as well as a dedication to inclusive and forward-looking policies.

Policymakers should concentrate on fostering innovation and technology breakthroughs in order to further improve the effectiveness and resilience of the financial system. Adopting digitalization and fintech technologies may improve customer experience, promote financial inclusion, and reduce procedures. To successfully manage risks and avert possible systemic crises, smart regulation should continue to be prioritized.

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CHAPTER 2

CLASSIFICATION OF FINANCIAL MARKETS

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ABSTRACT:

The financial market plays a crucial role in the global economy by facilitating the allocation of capital and enabling various financial instruments to be traded. This paper aims to explore the classification of financial markets based on different criteria. It provides an overview of the major types of financial markets, including money markets, capital markets, primary markets, and secondary markets. Furthermore, it delves into the distinctions between organized and over-the-counter markets, as well as the segmentation of markets based on the types of financial instruments traded, such as equity markets, debt markets, and derivatives markets. The classification of financial markets serves as a foundation for understanding the diverse nature of these markets, their underlying mechanisms, and the regulatory framework that governs them. By comprehending the characteristics and functions of each market type, investors and policymakers can make informed decisions and implement effective measures to ensure stability and efficiency in the financial system.

KEYWORDS:

Arbitrage, Bear Market, Bond, Capital, Commodity Market.

INTRODUCTION

Merchant Banking

All of these financial services provided by merchant bankers are included in fee-based consulting services.

Merchant bankers are crucial players in the financial services industry. In 1974, the Industrial Credit and Investment Corporation of India launched this service as the first organization providing development funding. The number of commercial banking organizations has greatly increased since the mid-1970s.

These consist of financial institutions including banks, non-banking financial firms, brokers, and so on. These companies provide financial services such loan syndication, portfolio management, project counseling for businesses, debenture trusteeship, and mergers and acquisitions[1], [2].

Credit Score

A credit rating is the rating agency's assessment of the issuer of a debt instrument's capacity and desire to pay back its debts when they become due.

Credit rating is helpful to investors, corporations, banks, and financial institutions as a fee-based financial advising service. It serves as a gauge of an issuance program's underlying credit quality for investors.

The investor has a complete understanding of the firm since the rating agency periodically assesses and publishes any effects that changes in business or economic circumstances have on the agency company[3], [4].

Securities trading

The Securities Contracts Regulation Act, which the Ministry of Finance enforced over stock exchanges, allowed for more or less self-regulatory organizations to operate until SEBI was established. When trading fraud became widespread, it became clear that stock exchanges needed to be improved. SEBI was established to make sure that stock exchanges fulfill their self-regulatory responsibilities effectively[5], [6]. Since then, stockbroking has developed into a respected advising industry. A stockbroker is a person who trades shares or other securities and is a member of a recognized stock exchange. Every stockbroker must register with SEBI in order to do business as a broker. When awarding the certificate of registration, SEBI has the authority to set restrictions[7], [8].

Financial Sector

The financial system of an economy operates via financial markets and institutions. The institutional arrangements for trading in financial assets and credit instruments of various forms, such as money, checks, bank deposits, bills, bonds, etc., are referred to as financial markets.The two financial markets are as follows:

Cash Market

The money market is a market where financial assets and securities with maturities of up to one year are traded. It is a market for just short-term investments, in other words[9], [10].

The following is a list of the money market's functions and importance:

1. Economic growth:

Both public and private entities may get short-term financing from the money market. These institutions need funding to cover their capital expenditures. In other words, the money market ensures the availability of cash; financing is provided by commercial banks, acceptance houses, discount houses, brokers, and the discounting of trade bills. The money market contributes to economic growth in this manner by giving trade, business, and industry financial support. Due to the ease with which these assets may be changed into cash, businesspeople profit by putting their wealth in highly liquid assets in order to generate revenue and enjoy liquidity.

2. Professional investment:

Commercial banks manage their clients' savings. The banks must convert their assets into cash in order to comply with the central bank's instructions, but they must also invest their surplus reserves in profitable ventures in order to generate money from them. The surplus reserves of the banks are invested in near money assets with the goal of maximizing returns.

3. Government borrowings:

The money market enables the government to get short-term loans at very cheap interest rates.

Treasury bills serve as the foundation for the borrowing. But if the government turns to deficit financing, increases currency printing, or uses short-term funds from the money supply in addition to borrowing from the central bank, it will only increase inflation. Therefore, it is evident that the economy's requirements and subsequently the price level would increase. Since it satisfies its financial demands, the money market is tremendously beneficial to the government.

4. Importance for the central bank:

The effective implementation of monetary policy by the central bank depends on the health of the money market. The only way the central bank can exert influence over the banking sector and so aid in the growth of trade and commerce is via the money market. The money market is very sensitive; any changes in one submarket have an instantaneous impact on the other submarkets. It implies that by altering only one sub-market, the central bank might have an impact on the whole money market.

5. Funds mobilization:

The money market aids in the movement of money from one industry to another. Any economy's growth is dependent on the availability of financing. Without the financial resources being mobilized, no nation can advance its trade, commerce, and industry.

6. Investing and saving

The money market contributes to the safety and liquidity of financial assets. By doing this, it may aid in promoting investment and saving.

The demand and supply of loanable money are in balance via saving and investment, which aids in the distribution of resources.

Financial Market

Financial assets with a protracted or undetermined maturity are traded on the capital market. It often deals with long-term securities having maturities longer than a year.Functions of the Capital Market A capital/security market primarily performs the following tasks:

1. Aids in the creation of capital

The capital market is crucial in helping to mobilize funds and direct them toward profitable investments that will advance trade and industry. As a result, the capital market aids in the nation's capital creation and economic expansion.

2. Serve conduit between investors and savers

The capital market serves as a crucial conduit between investors and savers. Investors are money borrowers, while savers are money lenders. The term "deficit units" refers to the borrowers while "surplus units" refers to the savers who do not spend their whole income. The transmission system between surplus and deficit units is the capital market. It serves as a conduit for surplus units to lend money to deficit ones.

3. Contributes to rising national income

The capital market receives funds from people and financial intermediaries, which are then employed by business, industry, and the government. Thus, it makes it easier to move money so that it may be utilized more profitably and productively to raise the national revenue.

4. Makes purchasing and selling easier.

Units with excess cash purchase securities, whereas those with deficit cash sell securities to raise money.

Directly or indirectly, money moves from lenders to borrowers via financial institutions like banks, unit trusts, mutual funds, etc. Primary securities are issued by the borrowers and are bought by lenders directly or indirectly through financial institutions.

5. Transfers money from ineffective to effective resources

If you have savings or need money for profitable investments, the capital market offers a market mechanism. It shifts resources away from wasteful and inefficient channels, such as extravagant spending and real estate, and into profitable investments.

6. Reduces speculation to a minimum.

It does this by lending money to those in need at fair interest rates and assisting in reducing speculative activity.

7. Brings stability to stock value.

The value of stocks and securities is stabilized by a well-developed capital market made up of knowledgeable non-banking and banking intermediaries.

8. Encourages economic expansion. The capital market fosters economic expansion. The many institutions that operate on the capital market provide the flow of money with quantitative and qualitative direction as well as a sensible distribution of resources. They do this by transforming financial assets into useful physical assets. This promotes the growth of business and industry in both the public and private sectors, which results in economic expansion.

New Issue Market / Primary Market

A primary market is one where fresh financial claims or issues are traded. As a result, it is also known as New Issue market. Securities that are originally released to the public are dealt with in the primary market.Borrowers trade brand-new financial instruments for long-term money in the main market. Therefore, the primary market aids in capital generation. A corporation may raise money in a main market in one of three methods.

DISCUSSION

This market is for fresh long-term equity funding. The main market is the one on which securities are first sold. Since the securities are offered by the firm directly to investors in a primary issue, it is also known as the new issue market. After receiving the funds, the business provides fresh security certificates to the investors. Companies utilize primary concerns to start new businesses, grow current businesses, or modernize existing businesses. The primary market plays a significant role in the economy by promoting capital creation. Some other long-term external financing sources, such loans from financial institutions, are not included in the new issue market. Going public, often known as turning private money into public capital, may be the goal of certain borrowers in the new issue market.

Fresh Issue Market's Purposes

Three service responsibilities

A new problem sues market's primary duties might be broken down into new projects.

1. Origination.

It alludes to the labor of reviewing, analyzing, and investigating fresh project ideas. It begins even before a product is officially put on the market. Merchant bankers, who may work for commercial banks, financial institutions serving all of India, or private businesses, perform this duty. Currently, financial institutions and private businesses both provide this crucial function. The effectiveness of the market has a significant role in the issue's success.

2. Underwriting.

In the event that the public chooses not to subscribe to the issue, the underwriter agrees to purchase a specific number of shares, debentures, or stock. The underwriter has no obligation if the issue is fully subscribed. The underwriter will purchase the shares if any portion of the share issuance is unclaimed. Thus, underwriting serves as a warranty that shares will be able to be sold. In India, there are two categories of underwriters: institutional and non-institutional.

3. Distribution.

Its purpose is to sell securities to major investors. Specialized organizations like brokers and agents that have frequent, direct touch with the end investors provide this service.

Primary Market

A secondary market is a market where securities are sold to other investors. In other words, shares traded in this market have previously been through the fresh issue market. These securities are often listed on the Stock Exchange, which offers a consistent and regular market for buying and selling stocks. All stock exchanges recognized by the Indian government are included in this market. The Securities Contracts Act of 1956 governs the stock markets in India. The primary stock exchange in India, the Bombay Stock Exchange, sets the standard for all other stock exchanges.

Activities of the Stock Exchange

An essential factor in a nation's economic growth is the stock exchanges. The following functions of the stock market will make evident how important they are: provide stock and shares a place to go

1. Ensure Capital Liquidity

the stock markets, where buyers and sellers trade goods and services for money. A ready market is offered by the exchanges. Had are always accessible, and individuals in need of immediate cash may sell their holdings. If this had been impossible, many people would have been afraid to invest their money in securities since they could not be converted back into cash.

2. An ongoing securities market

A ready market for securities is provided by the stock exchanges. Despite the fact that owners keep switching, stocks that were earlier listed continue to be traded at exchanges. A regular market for dealing in securities is offered by the exchanges.

3. Utilizing Extra Savings

Various securities may easily trade on the stock markets.

By buying shares, bonds, and other investments from the markets, investors may easily invest their resources. Many people who desire to invest their money won't have access to them if this facility doesn't exist. In this approach, stock markets are crucial for collecting investor excess cash.

4. Effective in Obtaining New Capital

Both new and old businesses need money for their operations. New concerns raise money for the first time, while older businesses raise more money for growth and diversification. New

businesses register their shares in stock exchanges, and established businesses also sell their shares there via brokers and other intermediaries. Exchanges aid in capital raising by netting both new and established firms.

5. Safety in Transactions

The Securities Contract Act of 1956 contains clear rules and regulations that regulate transactions at stock exchanges. Transactions that manipulate scope do not exist. Every transaction is carried out in accordance with the prescribed process, and neither party to the transaction feels afraid. The safety of transactions fosters trust in both parties and aids in the growth of diverse deals.

6. Securities listing.

At stock exchanges, only listed stocks may be acquired. Each firm that wants to list its securities must submit an application to the exchange authorities. Only after a thorough analysis of the company's capital structure, management, and prospects is the listing approved. The corporation gains privileges from the listing of securities. Because listing a security does not ensure the company's financial soundness, investors might make their own opinions about the securities.7. Evens out Price Movements.A stock exchange ensures a constant flow of securities, which smooths out price fluctuations of equities on the market.

8. Protection for investors.

Investors in securities get protecting services from the stock exchange. It offers investors a method for resolving complaints. A compensation fund is also run by stock exchanges for the benefit of investors.

Monetary Services Monetary Services

The caliber and range of financial services offered by financial intermediaries heavily influence the effectiveness of the developing financial system. Financial services are described as "activities, advantages, and pleasures associated with the sale of money, that provide users and customers with value that is financially related." Banks, financial institutions, and non-banking financial enterprises make up the three major segments of the financial services sector. Receivables make up a large amount of a company's current assets. However, a company must pay some expenses for investing in receivables, such as the cost of financing receivables and the expense of collecting on receivables. Having effective supervision and management of receivables is crucial since there is also a possibility of having debts. In actuality, sustaining receivables presents two different sorts of issues: the issue of obtaining financing for the receivables as well as the issues associated with collection, delays, and defaults of the receivables. A small business may be able to manage its receivables issues on its own, but a big business may not be able to do so effectively due to the danger of accumulating more and more bad debts. In such cases, a company may use the services of specialized organizations, or "factoring firms," that handle receivables.

Broadly speaking, factoring is the connection established by a contract between a seller of goods or services and a financial institution known as the factor, wherein the latter acquires the former's receivables and also controls and manages the latter's receivables. A continuous business relationship between a financial institution and a company that sells goods and/or renders services to a trade customer on an open account basis is known as factoring. In this relationship, the factor purchases the client's book debts with or without the client's consent, thereby controlling the credit extended to the customer and taking on the responsibility of managing the sales ledgers pertinent to the transaction.

The Factor's Functions

These are some of factor's functions:

1. Management of the sales ledger.

Each client's sales ledger is maintained by the factor. When a sales transaction is completed, the client prepares an invoice in two copies, sending one to the customer and the other to the factor. The open-item approach is used to make entries in the ledger.Each receipt is compared to the relevant invoice.

The client receives periodic reports from the factor on the current state of receivables and the total amount of money collected from clients. The frequency of the report is determined by the number of transactions. As a result, the factor assumes full responsibility for the client's sales ledger management.

Collection of Accounts Receivable

The primary duties include collecting receivables for the customer and relieving him of any hassles or issues related to collection. On the one hand, the customer may focus on other crucial aspects of his company, while on the other, labor, time, and effort savings help to lower the cost of collection.

3. Availability of Finance

The element makes finance, which is the lifeblood of a firm, readily accessible to the customer.

A factor buys the client's book debts, and the obligations are then allocated in the factor's favor. The factor gives the customer an advance of between 75 and 80 percent of the allotted obligations.

The factor becomes liable to the seller on the date of the invoice, whether or not the buyer makes the payment to the factor, if the client and the factor have an agreement in place for the purchase of receivables without recourse.

4. Defense Against Risk

When the debts are calculated without recourse, this service is offered. The factor determines the credit limitations for authorized clients and factors that fixed trade debt.In addition to relieving the client of collection duties, the factor also provides the client with advice on the creditworthiness of prospective clients.The criteria evaluate the customer's credit position based on data gathered from credit rating reports, bank records, trade references, and financial statements.

5. Consultative Services

These products and services result from a tight connection between a factor and a customer. Due to the fact that they have substantial credit, as well as superior expertise and experience in the area of finance Information on the status of the customer.

CONCLUSION

In conclusion, Understanding the complex and changing environment of financial systems requires a framework that helps classify financial markets. A good knowledge of the various markets that support the movement of money and financial instruments is provided by the classification based on several characteristics. Money markets are crucial to how financial

institutions and businesses handle their short-term funding and liquidity. On the other hand, capital markets are essential for long-term finance and investment prospects for governments and corporations.

The difference between the main and secondary markets draws attention to the process of issuing new securities as opposed to trading in already existing ones. Additionally, the distinction between over-the-counter marketplaces and established exchanges clarifies the various degrees of openness and regulation in various financial markets.

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CHAPTER 3

A STUDY ON ESSENTIAL ELEMENTS OF LEASING

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ABSTRACT:

Leasing has become a vital financing option for businesses and individuals worldwide. This paper examines the essential elements of leasing, a contractual arrangement that allows one party (the lessor) to grant the use of an asset to another party (the lessee) in exchange for regular payments over a specified period. The paper delves into the fundamental components of a lease, including the identification of the parties involved, the description of the leased asset, the determination of lease terms, and the calculation of lease payments. Additionally, it explores the different types of leases, such as operating leases and finance leases, and the accounting and taxation implications for both lessors and lessees. Understanding the essential elements of leasing is crucial for businesses and individuals seeking cost-effective and flexible means of accessing assets without the burden of ownership, making informed financial decisions, and complying with relevant accounting and tax regulations.

KEYWORDS:

Asset, Capital Lease, Depreciation, Equipment Lease, Finance, Gross Lease.

INTRODUCTION

Depending on the contract established between the selling business and the factor, a variety of factoring arrangements are conceivable. The collection of receivables and management of the sale ledger are the two aspects of factoring operations that are virtually universal. The primary sorts of factoring agreements[1], [2].

Factoring with recourse and without recourse

In a recourse factoring agreement, the factor has legal recourse against the client if the receivables bought turn out to be problematic; in other words, the client is responsible for the risk of bad debts and the factor does not take on the receivables' credit risks. As a result, the factor serves as an agent for bill collection and does not assume the risk of a customer's inability to pay a debt or the interest associated with it[3], [4]. As the seller assumes the risk of the buyer's credit and creditworthiness, the factor has the right to recoup the cash from the selling client in the event of such defaults.

The factor also assesses interest on the amount drawn by the customer for the time period in addition to charging the selling company for the upkeep of the sales ledger and debt collection services.

In contrast, non-recourse factoring requires the factor to assume any risk or loss due to the client's customers' failure to pay and forgoes his right to recover this money from the selling company.

The commission or fees paid for the services in the event of non-recourse factoring are greater than under recourse factoring since the factor assumes the risk of non-payment. Del credere commission is the name for the extra charge made by the factor in exchange for taking on the risk of bad debts or late payments at maturity[5], [6].

Factoring in Maturity

When debts are assigned under this category, the factor does not immediately pay the customer in cash. He promises to pay in cash as and when the debtors are collected from. The customer receives an instant payment of the total amount received minus factoring costs. As a result, it is also known as collection factoring. In actuality, there is no finance associated with this kind. All other services, however, are accessible.

Massive factoring

In this case, the factor offers financing after telling the relevant debtors that their obligations have been assigned. When the factor is not quite happy with the client's financial situation, they turn to this form of factoring. The customer must handle all administrative tasks for the sales ledger, including credit control, collection work, etc. The factor just collects the debts on behalf of the customer because notice has been given[7], [8]. Alternatively, this is referred to as "Disclosed Factoring" or "Notified Factoring."

Company Factoring

Regarding factoring, the term "agency" has no significance. In this instance, the client and the factor divide the task as follows:The client is responsible for managing the sales ledger and handling collections, while the factor is responsible for financing and taking on the credit risk.

Worldwide Factoring

This kind merely extends a factor's local business offerings to foreign commerce. Factoring is carried out solely on the basis of the exporter's invoice. Therefore, with international factoring, the exporter is able to get quick cash up to 80% of the export invoice. Export factors and import factors aid in the facilitation of international factoring[9], [10].

Factoring with Suppliers' Guarantee

This kind of factoring is appropriate for companies who sell their products via intermediaries. In general, commodities are sold via intermediaries, merchants, or wholesalers. In these situations, the factor backs up the product supplier against invoices submitted by the product provider to another product supplier. The factor who guarantees payment of the invoices receives an assignment of the bills. As a result, the provider may generate profits with little financial investment.

Small-scale factoring

With this kind, the factor does not purchase all of a client's bills. He only offers merit-based reductions on a limited number of invoices, and he only turns credit bills for those invoices into cash.

Factoring based on purchases

The component often represents the seller as an agent. However, in this case, the buyer goes to a factor to have his expenses discounted. Therefore, factoring is a decision that is made by the buyers. A factor is contacted by a company's authorized customers in order to get a discount on their invoices. In these situations, without the seller's involvement, the claims against such customers are settled by discounting the invoices, and the seller also receives ready cash. This facility is known as "selected" since it is only offered to reputable, credit-worthy consumers. Seller-based and Buyer-based Factoring.

In this case, after billing the consumers, the seller sells all of his accounts receivable to the factor rather than discounting his invoices. Once he creates the invoices, the seller's work is done. The factor then assumes responsibility for the remaining tasks after receiving all the sale-related documentation. Since only reputable and creditworthy merchants are given access to this service, it is also known as Selected Seller Based Factoring.

Leasing

The basic goal of a company is to maximize the financial well-being of the owner. The company looks at numerous funding options for appealing projects after finding them, with the goal of maximizing shareholder value. Leasing has become a third significant form of intermediate and long-term financing of business companies during the last several decades, in addition to debt and equity financing. In western nations, it is often utilized to fund investments. Leasing before 1950 mostly dealt with real estate, i.e., land and buildings. However, practically all fixed asset categories are now capable of being leased. Leasing is a relatively new phenomenon in India, and First Leasing Company of India Limited was the first to provide equipment leasing. Since then, a number of medium- to large-sized businesses and financial institutions have also joined the leasing industry. Leasing is a contract that allows a company to utilize and manage assets without purchasing and owning them. It is a kind of asset rental. A lease is a contract in which the asset's owner, known as the lessor, grants the lessee the right to use the item for a certain amount of time in exchange for a sum known as the lease rental. The terms and circumstances of the agreement govern the leasing arrangement. The lessor receives periodic fixed payments from the lessee for the lease tent over a period of time. The rent may be due at the start or conclusion of each month, quarter, half-year, or year. According on the lessee's profitability and cash flow situation, the quantity and timing of the lease rentals may also be agreed upon. The asset returns to the lessor, who is the rightful owner of the asset, at the end of the lease term.

Important Components of Leasing

1. The number of contracting parties. A lease finance deal always has two parties.

The consumer or lessee the lessee or the owner

2. **Asset:** An asset, piece of property equipment, such as plant and machinery, real estate, a building, etc., may be the subject of a lease finance arrangement.

3.**Consideration:**For a sum of money known as lease rental, the lessee is granted access to an asset. The lessor calculates lease rent by taking into account the capital invested in the asset, depreciation, capital interest, repairs, etc.

4. **Leasable Term:**Typically, a lease is signed for a certain amount of time. On occasion, it could extend across the whole of the asset's economic or functional life. The asset reverts to the lesser, who is the actual owner of the asset, at the end of the lease term.

5. **UseOwnership, VIS:** While the lease is in effect, the lessor continues to be the asset's owner while the lessee is in possession of it. During the term of the lease agreement, he may utilize the asset.

Lease for operation or services

The following characteristics often define an operational lease:

It is a brief lease that lasts from one period to the next. In such a deal, the lease term is less than the asset's useful life. The lessee often has the right to terminate the lease with little

notice. An operational lease does not always amortize the asset's initial cost since its term is less than its useful life. To recoup his cost of investment and desired rate of return, the lessor must lease the item out again or sell it. After the initial lease time expires, the lessee often has the option of renewing the lease. Generally speaking, the lessor is in charge of the asset's upkeep, insurance, and taxes. He might offer the lessee other services as well. Given that it is a short-term, cancellable lease, the lessor is exposed to more risk, while the lessee is subject to higher lease payments. For equipment that needs professional technical maintenance and is subject to technological advancements, such as computers and cars, operating or service leasing is popular.

DISCUSSION

Financial Lease

If a lease guarantees the lessor's term for the amortization of the whole cost of the investment together with the anticipated return on capital expenditure throughout the length of the lease, it is defined as a financial lease. These leases are typically for a longer term and are non-cancelable. Financial leases are a kind of funding that is comparable to debt finance. Financial leases, which are often used to lease land, buildings, machinery, and fixed equipment, make up the majority of leases in India.A financial lease often has the following characteristics: The total lease rents due during the term of the lease have a present value that is more than or equal to almost the whole fair value of the leased item. It means that the lessor will make back his investment in the asset and earn an accept rate of return throughout the term of the lease.A financial lease is for a longer length of time than an operational lease. Prior to the lease's expiry date, the lessee often cannot terminate it. In general, the lessee is in charge of the asset's upkeep, insurance, and servicing. However, in rare circumstances, the lease agreement's conditions may mandate that the lessor maintain and service the asset. 'Maintenance or gross lease' is the term used to describe such a contract. A financial lease often gives the lessee the option of extending the lease at a low cost.

Financial lease agreements' many forms:

The main types of financial leasing agreements are as follows:

Buyback and sale. An asset that a company already owns is sold in a sale and leaseback agreement, and the buyer then leases the item back to the seller. In exchange for regular lease payments, this kind of lease agreement allows a business to keep economic use of an asset while simultaneously receiving income from the sale of the asset. Businesses that need working capital funds often choose a sale and leaseback agreement. Insurance firms, pension funds, private finance businesses, and financial institutions are some of the lessors that participate in sale and leaseback transactionsleasing directly. In direct leasing, as opposed to sale and leaseback, a company makes use of an asset that it does not already own. Direct lease arrangements may be made with the manufacturer or supplier or via the leasing firm.

In the first scenario, the manufacturer or supplier serves as the lessor personally, but in the second scenario, the lessee company arranges for the leasing business to acquire the asset from the manufacturer or supplier and also enters into a lease arrangement with the lessor for the asset.

Lease leveraged. In a leveraged lease, the lessor borrows money from a third party, the lender, who is often a bank or financial business, to pay for the asset. The asset's mortgage and the lease rents that will be paid by the lessee often serve as security for the loan. The loan is repaid out of the lease payments, sometimes straight from the lessee to the lessor by paying

just the surplus sums. The lender is often a bank, insurance company, financial institution, or a private finance organization, while the lessor serves as both the owner and the borrowerbotha straight and modified lease. The difference between a straight lease and a modified lease is that a straight lease requires the lessee company to pay lease rents during the asset's anticipated service life and does not allow for any changes to the basic lease's terms and conditions. For instance, the option to end the lease might be made available by either buying the item or giving it back.

Secondary and Primary Lease

In a main and secondary lease, the lease rents are calculated such that, during the first term of the lease, the owner recovers the cost of the asset and accrued profit before a secondary lease is offered at minimal fees. Simply put, the rents charged during the main period are much higher than those paid during the secondary term. These types of lease agreements are sometimes referred to as front- and back-ended leases.

Other Lease Types

Lease Agreements with Floating Rental Rates. This kind of leasing arrangement was brought about by the frequent variations in interest rates over the last several years. Lease rents under this sort of lease are altered by the lessor in accordance with borrowing rates. This kind of lease agreement enables the lessee to assume the risk and profit from changes in interest rates.

International and domestic leases

A domestic lease is one in which the parties involved are all citizens of the same nation: the lessor, lessee, and the equipment provider. International leasing is used when the parties to the lease agreement reside in separate nations.

There are two types:

Lease an import. In this kind of lease, the equipment provider comes from a different country than the lessor and lessee, who both reside in the same nation. The equipment is initially imported by the lessor, who then rents it to the lessee.International Lease. Cross-Border leasing is the practice of renting out equipment to a lessee who is not subject to the laws of the lessor's nation; the supplier's domicile is irrelevant in this situation.

Aid - Sale Leasing. A manufacturer extends a facility of leasing directly under this form of leasing, either via one of his own subsidiaries or a third party.

A manufacturer may have direct communication with the consumer via leasing, guarantee that the equipment is regularly updated or replaced, and boost sales.

The lessee also has a significant benefit since he pays for the item on a monthly payment basis over a very long period of time. Without spending any funds, he installs and activates the asset.

Consumer Lending

Consumer Finance/Consumer Credit refers to any asset-based lending options made available to people to assist them in purchasing durable consumer items. In a transaction involving consumer credit, the person, consumer, or buyer pays a portion of the cash purchase price at the time the item is delivered and pays the remaining amount with interest over a certain period of time.

Benefits and Importance of Consumer Finance

Consumer durables including automobiles, refrigerators, TVs, radios, typewriters, sewing machines, electrical appliances, and many more things are produced in large quantities and distributed to consumers. Giving customers credit is a huge convenience. Furthermore, credit now plays a significant role in the competitive economy of today. It serves as a marketing tool and a great way to promote sales.

The following justifications may be made for consumers of consumer finance:

Enjoying the Benefits of Possession. The ability to hold products without having to pay for them right now is a significant advantage of consumer credit. The consumer does not need to wait and save money in order to get the thing of their dreams. Mandatory Saving. Using consumer credit offers a tool for required saving. People are compelled to use their wealth more wisely as a result of this. It encourages thrift among individuals and makes it possible for those with low resources to buy items. Simple Method of Purchase. Consumer durables may be purchased easily using consumer credit under the open account system. to provide for urgent needs. When faced with unexpected costs associated with sickness, accident, or death, consumer credit may help. Additionally, in desperate situations, this aids in preserving the customer's respect. Increase in Revenue. Without a credit option available to clients, commodities that would have stayed unsold may now be quickly disposed of. More business is prompted by credit. Regarding non-essential or luxury items like vehicles, trucks, refrigerators, typewriters, all types of electrical equipment, TV sets, sewing machines, etc., this is definitely the case. Therefore, via credit sales, producers and dealers may ensure continuously rising sales and profits. Dream realization. A customer who may enjoy the ownership of goods without paying for them right away benefits from consumer credit. Spreading out the payments over a certain time period in the future makes it convenient. Consumers are able to set aside money from their regular, fixed, and finite income to budget for the purchase of even pricey capital goods.

1. Auto financing

Everybody wants to possess a car in this day of rapid living and the shifting paradigms in society. As a result, vehicle loans have become necessary since those without adequate finances choose to purchase now and pay later. Every antique two-wheeler, used automobile, and new car may be financed under the banks' auto loan program. The market for vehicle loans is huge, and there are many opportunities there for banks and other financial institutions, which may make auto lending schemes a success by implementing customer-friendly rules and extensive promotion.

Eligibility. Government, public, and private sector permanent workers with a minimum of three years of service are eligible for auto loans. professionals and independent contractors including physicians, actuaries, company secretaries, architects, engineers, and MBAs, among others. those who work in agriculture and related fields. Purpose. For the purchase of a car, both for personal and business use, auto loans are made available. Loan kind. Term loans with terms ranging from one to five years are one way that money is made available. Interest Rate. Interest rates differ from bank to bank. Security. Every bank request the hypothecation of the financed vehicle. Insurance. Every car has insurance. A thorough insurance coverage is obtained for the greater of market value or 10% more than the loan balance.

The policy makes notice of the bank's interests. Processional Fees. Most banks don't impose any processing fees, however 250 to 500 may be taken from consumers once. Price

reductions. Some banks provide their clients with a variety of discounts in any of the following ways:

Customers who apply for a loan for more than one automobile or who already have an auto loan are eligible for a volume discount of 0.5%. to the great performance of previous Relationship discounts of 1.0% may be provided to applicants who keep acceptable current or savings bank accounts for at least three months, customers who have an equal number of FDs with bank liens noted, and applicants who maintain satisfactory term loan accounts or working capital accounts.

Customers with good credit who have maintained excellent accounts for at least 12 months, have a clean credit card history, and have paid off prior automobile or two-wheeler loans on time may be eligible for a 1.0% good credit discount.

A 1.0% income discount is provided to candidates whose income exceeds a specific threshold. Bank of Punjab, for instance, has restrictions:

For a typical sector auto loan, pay Rs. 1,000,000 for a middle-segment auto loan, Rs 1,20,000 For a premium sector auto loan, pay Rs. 140,000 Doctors get a 10% professional discount. CAs and professors.

Institutions for Regulation

Under the guidelines of the Reserve Bank of India Act, 1934, the Reserve Bank of India was founded in Calcutta in 1935 and later relocated permanently to Mumbai. Despite being privately held at first, was nationalized in 1949.

Organization and Management:

A central board of directors oversees all operations of the Reserve Bank. In accordance with the Reserve Bank of India Act, the board is appointed by the Indian government for a term of four years. Governor and a maximum of four Deputy Governors are the only full-time representatives.

The Reserve Bank of India typically carries out the following significant tasks:

1. Rupees Problem:

As the nation's central bank, the RBI is given the only ability to print currency notes after maintaining a minimum reserve of gold worth Rs. 115 crore and foreign currency worth Rs. 85 crores.

Later, this clause was cleaned up and modified.

2. Banker to the Government:

Since the RBI serves as the government's banker, all monies belonging to the federal and state governments are stored there. It oversees the nation's public debt and serves as the government's representative. Additionally, the RBI is providing short-term "ways and means advance" to the government.

3. Banker's Bank:

The RBI also serves as the country's banker for other banks. It oversees the whole nation's banking system, maintains a certain proportion of deposits as a minimum reserve, serves as the last-resort lender for its scheduled banks, and runs clearinghouses for all other banks.

4. Credit Control:

By using both quantitative and qualitative credit control methods, such as fluctuation in bank rates, open market operations, selective credit restrictions, etc., the RBI is given the exclusive right to manage the credit issued by commercial banks.

5. Custodian of Foreign Exchange Reserves:

The RBI is given exclusive control over setting the exchange rate between the rupee and other foreign currencies and is also responsible for maintaining the government's earned foreign currency reserve. The International Monetary Fund and the RBI continue to have a relationship.

6. Developmental Activities:

The RBI also performs development activities by fostering the growth of a number of sister organizations, such as the Agricultural Refinance Development Corporation. Indian Industrial Development Bank, among others, for providing agricultural and industrial financing across the nation. When NABARD was founded on July 12, 1986, ARDC's whole mandate was transferred to it. The Reserve Bank of India has contributed half of NABARD's share capital. As a result, the Reserve Bank serves a valuable purpose for overseeing and administering the nation's overall banking, monetary, and financial system.

CONCLUSION

In conclusion, Businesses and individuals may make wise financial choices, maximize asset usage, and successfully negotiate the complexity of accounting and tax requirements with the help of a thorough grasp of the fundamentals of leasing. Leasing will remain a substantial and important financing option for addressing a variety of asset demands in a more competitive and dynamic corporate environment as it continues to change. Leasing has many advantages, but it also has dangers and difficulties, such as residual value uncertainty, prospective maintenance obligations, and the need to carefully assess the lessor's financial soundness. Therefore, it is essential for all parties engaged in a lease to do extensive due diligence and comprehend all lease conditions.

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CHAPTER 4

REGULATORY AND PROMOTIONAL ROLES OF RESERVE BANK OF INDIA

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ABSTRACT:

The Reserve Bank of India (RBI) serves as the central bank and apex monetary authority of India. This paper examines the regulatory and promotional roles played by the RBI in the Indian economy.

The regulatory functions encompass the supervision and control of the country's banking and financial system, including commercial banks, non-banking financial institutions, and payment systems.

The RBI plays a crucial role in maintaining financial stability, enforcing prudential norms, and safeguarding the interests of depositors and consumers.

Additionally, the paper explores the RBI's promotional roles, which involve fostering economic growth, monetary policy implementation, and developing a robust financial infrastructure.

As a key player in India's financial landscape, the RBI's dual responsibilities of regulation and promotion contribute significantly to the stability and progress of the nation's economy.

KEYWORDS:

Banking Regulation, Currency Management, Financial Stability, Foreign Exchange, Inflation Control, Monetary Policy.

INTRODUCTION

In terms of regulation and promotion, the Reserve Bank of India has been a significant player in the Indian economy. Developmental activities have accelerated throughout the nation since planning began in 1951.

As a result, the RBI has been given an increasing number of duties in both the regulatory and promotional fields. Today, the RBI serves the nation in a variety of regulatory and promotional capacities[1], [2].

Some of the regulatory and marketing tasks carried out by the RBI include the following:

1. Controlling the amount of money:

its Issue Department, the RBI regulates and administers the whole amount of money in the nation. The demand for currency and the stability of the economy are both given equal weight by the RBI while controlling the amount of currency[3], [4].

2. Controlling Credit:

Through its qualitative and quantitative techniques of credit management, the RBI also plays the duty of regulating the credit money issued by the commercial banks, helping to keep the nation's money supply in check[5], [6].

3. Control over Commercial Banks:

The RBI also serves as a regulator by exercising control over how commercial banks operate. Additionally, it imposes prudential standards and sensible banking practices on the commercial banks.

4. Formulating the Monetary and Credit Policy:

The RBI formulates the nation's monetary and credit policy each year, consequently regulating the Statutory Liquidity Ratio, Cash Reserve Ratio, Bank Rate, Interest Rate, Credit to Priority Sectors, etc.

5. Mobilizing Savings:

Through its member commercial banks and other financial institutions, the RBI is playing a crucial promotional role to mobilize savings. Additionally, RBI is advising commercial banks on how to expand their banking services into unbanked rural and semi-urban regions as well as how to encourage individuals to open bank accounts. All of these have helped the economy become more monetized and have been successful in reducing the activity of local bankers and private moneylenders[7], [8].

6. Institutional Credit to agricultural:

Since the inception, the RBI has worked to boost the flow of institutional credit to agricultural. The RBI established ARDC in 1963 to fulfill the long-term lending needs of rural communities with this goal in mind. The RBI then established NABARD and combined ARDC with it to handle its agricultural lending operations in July 1982.

7. Specialized Financial Institutions:

The RBI has also been actively promoting the establishment of specialized financial institutions to address the long-term lending requirements of various industries, both big and small.

As a result, the RBI has encouraged the growth of several financial institutions, including as WCI, 1DBI, ICICI, SIDBI, SFCs, Exim Bank, etc., that have a substantial impact on the nation's industry and commerce[9], [10].

8. Depositor security:

In 1962, the RBI took the lead in establishing the Deposit Insurance Corporation of India in order to overcome the main barrier to deposit mobilization caused by repeated bank failures. The primary goal of this organization is to provide depositors protection from such failures.

9. Advisory Roles:

The RBI also serves as an adviser to the Central and State Governments on financial issues as well as on broader economic issues.

10. Policy Support:

The RBI also actively supports government policy by doing research on the nation's most pressing economic challenges and concerns. This aids the government in developing its economic policies in the most logical way possible.

Thus, it can be seen that the RBI, via its regulatory and promotional framework, has been actively contributing to the nation's economic progress.

Indian Securities and Exchange Board

In light of these conditions, the government decided that an apex organization needed to be established in order to grow and oversee the Indian stock market. The Securities and Exchange Board of India eventually was decided upon on April 12, 1998. SEBI was initially established as a non-statutory entity. It took the government close to four years to enact a separate piece of legislation with the Securities and Exchange Board of India Act 1992, which granted statutory authority. The Act granted SEBI broad authority over almost all facets of capital market activities.

Goals of the SEBI

The main goals of the SEBI are to encourage the securities market's wholesome and orderly expansion and to provide investor protection, according to the preamble of the SEBI Act. The SEBI keeps an eye on merchant bankers, stock exchanges, and other businesses for this reason. The following are SEBI's goals:

1. To safeguard investors' interests and maintain a constant inflow of funds into the capital market.
2. To control the securities market and guarantee that issuers of securities operate fairly in order to raise funds at the lowest possible cost.
3. To encourage brokers, merchant bankers, and other intermediaries to provide effective services in order to boost their professionalism and competitiveness.

DISCUSSION

Mutual Funds and Venture Capital Mutual Fund

Millions of individuals throughout the globe now choose mutual funds as their top investment choice. The ‘safety of the principal' promise, together with the bonus of capital appreciation and the income received in the form of interest or dividend, are what motivate mutual funds. People like mutual funds over bank accounts, life insurance, and even bonds since they can start investing with minimal capital. Simply put, a mutual fund gathers small participants' funds, invests them in government and other corporate assets, and generates income through interest and dividends in addition to capital gains.

Diversification in Mutual Funds is Important

Many investors carry tiny sums of money with them. They are only able to purchase shares in one or two businesses. Small savings may be utilized to purchase shares in several firms when they are pooled and given to mutual funds. As a result, investors may take part in a large basket of shares from various firms.

Liquidity

Investments made in a mutual fund's plans provide a distinctive benefit: may be quickly turned back into cash without expensive brokerage, delays, etc. costs. A mutual fund is needed in India to guarantee liquidity, per SEBI requirements. The investor may always ask the Mutual Fund to repurchase units at the stated asset value in the case of open-ended schemes. The stock market makes it simple to sell in the event of a closure. finished plans, units

Lower Risk.

The risk element for the investor is decreased by mutual funds' extensive investments in a variety of businesses and their expert management. On the other side, a small investment may

not be able to reduce such risks. tax benefit. Certain mutual fund programs provide lenient advantages in accordance with the Income Tax Act. As a result, when an individual invests in these mutual fund schemes, his tax burden is also decreased.

Low expenses of operation

Because mutual funds have a lot of investable money at their disposal, they may benefit from large-scale economics. As a result, they may operate at a lower brokerage, fee, commission, etc. cost. As a result, a small investor also benefits from economies of scale and reduced operational expenses.

Flexibility.

Mutual funds provide its members a variety of flexible investment plans, including regular investment plans, regular withdrawal plans, and dividend reinvestment plans, among others. As a result, an investor may invest or withdraw money in accordance with his own needs,

Increased Returns.

A larger return is anticipated from mutual funds than from direct investments due to their expert management, scalability, lower risk, etc.

Investor Defense.

The Securities and Exchange Board of India oversees and regulates mutual funds. The SEBI Mutual Funds) restrictions, 1996 which superseded the restrictions from 1993 offer investors improved protection, more flexibility, and a competitive advantage.

Mutual Fund Types

Closed-off Funds

The fund's corpus and term are specified under this arrangement. In other words, the fund's corpus and the total number of units are predetermined. Investor entrance is closed after the subscription reaches the pre-determined threshold. The whole corpus is disinvested when the predetermined time has passed, and the profits are divided to the individual unit holders in accordance with their respective holdings. After the last payout, the fund no longer exists as a fund.characteristics: The close-ended funds' primary characteristics include:

The duration and/or goal amount of the fund are predetermined and defined in advance. The door is shut for investors after the time period has passed or the goal has been attained. They are unable to buy any more units.

There is often no buyback facility by the fund; these units are openly traded on stock exchanges. Capital growth is the primary goal of this fund.

Open-ended Investments

This is the complete opposite of closed-end funds. The amount and/or duration of the fund are not pre-determined under this system. Any number of units may be purchased or sold at any moment by investors. This unit is available for purchase by anybody at any moment, and anyone may sell it at any time as well.

The Open-Ended Funds' Key Characteristics are:

Regarding investments and withdrawals, there is total freedom. In other words, investors may freely enter and depart an open-ended fund. No time restriction applies. The investor has the

flexibility to join and leave the Fund whenever he chooses. Although these units are not traded publicly, the Fund is prepared to buy and sell them at any moment. Instant liquidity is made available to the investor in the sense that the units may be sold to the Fund at any time during business hours. This fund's primary goal is to generate revenue. As compensation for their investment, investors get dividends, rights, or bonuses. The units' pricing are based on their Net Asset Value since they are not listed on the stock market. The Fund decides the NAV, and it changes periodically.

Considering Income

A) Income Funds: As the name implies, this fund's goal is to generate and distribute recurring income to its members on a basis that yields larger returns than periodic. It focuses more on how income is distributed and considers how much money is earned on average from bank deposits.The investor is guaranteed a consistent income at regular times. say every half year, every year, and so forth. This kind of Fund's primary goal is to regularly issue dividends, not capital appreciation. The investing pattern favors assets with high fixed income yields, such as bonds and debentures. The elderly and retired who may not have a regular income are most suited for this. Funds for pure growth. Growth funds, as opposed to Income funds, focus primarily on long-term returns, or capital appreciation. They don't provide consistent income, and their long-term goal is capital growth. They are thus referred to as " Nest Eggs " investments.

The goal of the growth-oriented Fund is to satisfy investors' desire for capital growth. As a result, by focusing primarily on stocks with significant growth potential, the investment strategy complies with the Fund's purpose. The Fund invests in high growth equity shares and risk-bearing stocks in an effort to increase its capital. Although the fund may distribute dividends, its main goal is to increase in value. This is best suited to salaried and corporate individuals with high risk tolerance and cash deferral capability. They are able to amass riches to meet future requirements.

Equilibrium Funds:

This is also known as the "income-cumulative-growth" fund. It is nothing more than a blend of growth and income funds. It seeks to distribute both normal income and capital gains. This is accomplished by distributing the investments between fixed income-earning assets and high-growth equity shares.

Specialized Funds:

These funds invest in a certain class of assets; they may focus on securities issued by businesses that deal in a specific kind of product or service, businesses in a specific sector, or securities that generate a specified amount of income. An investor who wants to invest in a certain asset will choose a fund that deals in that security.

Money-Market Mutual Funds:

These funds have all the characteristics of an open-ended mutual fund since they are essentially one. However, they make investments in very liquid and secure assets like Treasury bills, commercial paper, banker's acceptances, certificates of deposits, etc. Money market instruments are what these things are called. In a capital market, they stand in for shares, debentures, and bonds. They pay interest at money market rates. Taxation Funds: A taxation fund is essentially a fund that is focused on growth. However, it provides tax advantages to investors in both the local and international capital markets. Salary persons who wish to benefit from tax refunds, especially in the months of February and March,

should do so. In India, Section 88 of the Income Tax Act, 1961 now governs the rules pertaining to tax refunds. For contributions made via this fund, an investor is eligible for a 20% income tax credit, up to a maximum of Rs. 10,000 per year.

Classification Other

Loaned Money:

Since they are generally used to expand the size of a mutual fund's portfolio's value, these funds are also known as borrowed funds. The fund's ability to make more money rises along with its value. This is only used when the profits from the borrowed money exceed the cost of borrowing funds. The gains are paid to the unit holders. Dual Funds are a unique kind of closed-end fund. It gives two distinct sorts of investors a single investment opportunity. It offers income shares and capital shares, two different forms of investment securities, for this purpose. Investors looking for immediate returns on their investments might buy income shares. All interest and dividends from the whole investment portfolio are paid to them. They do, however, get a minimum yearly dividend payment guarantee. Capital share owners get all capital gains made on their shares, but they are not eligible for any kind of dividend. The dual fund and a balanced fund are distinct from one another in this regard.Index funds are those funds whose portfolios are constructed in a manner that they accurately mirror the makeup of a wide market index. Holding securities in the same ratio as the index itself achieves this. When the market index rises, the value of these index-linked funds will rise automatically, and vice versa.

Bond Funds: The portfolios of these funds are mostly made up of fixed income instruments, such as bonds. These funds' primary focus is mostly on income rather than capital gains. In contrast to income funds, they provide capital gains that are lower than those from equity shares and average returns that are larger than those from bank deposits.

Investment Concept of Investment

It's possible to interpret the phrase "venture capital" in a number of different ways. In a more limited sense, it refers to investments made in fresh and tried-and-true businesses without a track record of expansion. Venture capital, in a larger sense, refers to the commitment of funds in the form of stock for the creation and establishment of small businesses that specialize in novel concepts or emerging technology. It is not only a financial investment; it is also a simultaneous input of the skills required to establish the organization, create its marketing plan, and organize and manage it. It is an affiliation between the many phases of a company's growth and unique funding options suitable for each level of development.

Venture Capital Definition

Venture money is long-term risk capital used to fund high-technology enterprises with risk and significant growth potential. Venture capitalists combine their resources, including their management skills, to support beginning companies. When the project becomes profitable, they sell their share stakes at a significant profit.

Types of venture capital, their stages, and their purpose

At various phases of the project, venture money may take many different forms. A project goes through four phases in succession, from conception to implementation to commercial production and marketing to large-scale investment to take advantage of scale economies and create stability. Banks and other financial institutions seldom begin project funding at the first

stage but instead wait until the second or third stage. However, venture capitalists provide funding even at the ideation stage.

The many phases of venture capital funding are described:

1. Seed funding for idea development

Venture capitalists provide seed money during the early stages of turning an idea into a business proposal. At this step, an extensive study is conducted, which often takes a year or more.

3. **Implementation Stage**

Start Up Finance: The venture capitalists give start up financing when the company is established to produce a product or provide a service. First- and second-stage capital are utilized for full-scale production and subsequent company expansion.

Fledging Stage

Additional Finance: In the third stage, the company has achieved some progress and has moved on to the product production stage, but there are still some growing pains. It may not be able to raise enough money, thus extra finance is given to build the marketing infrastructure.

Establishment Finance: At this point, the company is well-established in the industry and is anticipated to see substantial growth. It needs more funding for growth and diversification in order to benefit from economies of scale and achieve stability. The company is listed on the stock market at the conclusion of the establishment stage, and at this time the venture investor sells their shares through the legal channels that are available.

CONCLUSION

In conclusion, The Reserve Bank of India is still a dependable organization that faithfully performs its regulatory and promotional duties to make sure that India's financial system is strong, robust, and dynamic. Being a key participant in India's quest for sustainable growth and prosperity, it continues to impact the country's economic trajectory via its cautious policies and forward-thinking outlook. The RBI's adaptable and proactive approach will continue to be crucial in handling upcoming difficulties and opportunities as the economic environment changes. For the Indian economy to continue to expand and remain stable, the RBI's ability to strike a careful balance between its regulatory and promotional responsibilities is essential. The management of the effects of the world's economic uncertainty, dealing with non-performing loans in the banking industry, and promoting sustainable and equitable development are still obstacles.

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CHAPTER 5

CONSTITUENTS OF INDIAN MONEY MARKET

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ABSTRACT:

The Indian money market plays a crucial role in the financial system, providing a platform for the exchange of short-term funds and facilitating liquidity management for various entities. This paper examines the constituents of the Indian money market, which include the Reserve Bank of India (RBI), commercial banks, non-banking financial companies (NBFCs), and other financial institutions. It delves into the key money market instruments such as Treasury Bills, Commercial Papers, Certificates of Deposit, and Repurchase Agreements (Repos), along with the role of the money market in influencing monetary policy and regulating liquidity in the economy. Understanding the constituents of the Indian money market is essential for policymakers, investors, and financial institutions to make informed decisions and maintain stability in the financial system.

KEYWORDS:

Call Money, Certificate of Deposit (CD), Collateralized Borrowing,Credit Rating, Interbank

INTRODUCTION

Through the creation of commodities and services and their efficient distribution, an economy may contribute to the wellbeing of its citizens. The provision of products and services, as well as their distribution, are fundamental economic activity. The methods and means by which the financial system may provide support to the actual sectors for their operation and expansion make up its financial system. Services, markets, and institutions make up the financial system.

It includes everything from credit unions, payday loan firms, banks, insurance providers, investment trusts, and stock exchanges. Coins, currency notes, checks, bills, bonds, stocks, futures, and swaps are just a few of the instruments it uses. There are both established and informal markets for financial instruments, including the money market, the capital market, and others.

A financial system also offers services that are crucial for the nation's economic growth. As a result, it is argued that finance, credit, and money are an economy's lifeblood. When resources are available, a strong financial system may help an economy grow quickly. The financial system is made up of a number of institutions, markets, and tools that are connected in a systematic way and serve as the main channel for converting savings into investments. Every nation has both specialized and non-specialized financial institutions that make up its financial system.

It also includes both established and uncontrolled money markets, which use financial instruments to provide services and make money transfers easier. S.B. Gupta asserts that the "financial system is a set of institutional arrangements through which the financial surpluses available in the economy are mobilized." The definitions mentioned above call our attention to the following details. elements of the financial system. features of the financial system's structure, and the financial system's functions[1], [2].

The Financial System's Organization

The financial system's structure is straightforward and limited in scope, consisting of sections and sub-components. Due to its extensive network and variety of instruments, the financial system's structure is becoming more complicated in the contemporary economy[3], [4].

The financial system's structure consists of both ordered and disorganized elements. The organized part comprises of several institutions that provide depositors a variety of options for lending their money. Bank deposits, P.O. deposits, corporate deposits, shares, debentures, insurance policies, units of UTI, etc. are examples of financial assets in an organized system[5], [6].

Inter-relationships:

Understanding how the financial system is structured can help you better comprehend its internal connections. For instance, 'core' institutions like commercial banks participate in both the money market and the capital market. As a result, the interest rates of funds for various time periods are closely related. Similar to it, there are nearby markets. Financial assets are interdependent, meaning that suppliers have a variety of options, including shares, corporate deposits, P.O. deposits, insurance policies, and bank deposits[7], [8]. Additionally, the financial system encourages individuals to invest their excess in financial assets. People who own idle assets, for instance, may turn them into tangible assets, such as real estate or other assets. The RBI monitors or controls the banks' contribution to the production of credit. The financial system's structure: The following components make up the financial system's structure: Institutions of finance. monetary markets.

Services and Financial Instruments

Institutions of finance are sometimes referred to as intermediates. These organizations go by the names of institutions and non-banking organizations. Commercial banks and cooperative banks make up the banking system in India. Life Insurance Corporation, Unit Trust of India, and Industrial Development Bank of India are examples of non-banking organizations. Between investors and savers, these financial intermediaries act as an intermediary. They both mobilize funds and provide loans. Their assets come from investors or loans, but their responsibilities are to the final savers. Non-intermediaries do lean business, but they do not acquire their resources directly from savers[9], [10].

Financial Markets: The financial system is supported by financial institutions and markets. "A center that offers facilities for buying and selling of financial claims and services" is what a financial market is. The financial instruments covered include money, deposits, checks, bills, and bonds. Financial markets are quite similar to markets for commodities and services analytically. They have two sides: the supply of money and the demand for it.

Primary and Secondary Markets: New financial claims or securities are traded in the primary markets. They also go by the name "New Issue Market." The secondary market deals with already-issued, already-existing, and still-expiring securities. Primary markets provide company units with new money. Secondary markets provide the business unit with financing in an indirect manner.

Money and capital markets: Money and capital markets are subcategories of the financial market. Because both markets serve the same purpose of delivering financial resources to businesspeople or producers, there are no significant differences between them. Short-term claims are dealt with in the money market. Short-term claims are dealt with in the capital market.

Organized and Unorganised: Organized markets are tightly interconnected. Foreign banks, cooperative banks, commercial banks, other financial institutions, mutual funds, etc. are all included. The RBI is the country's top financial institution.The money market's unorganized sector is made up of local bankers, money lenders, and unregulated non-bank financial intermediaries including chit funds and niches.

Services and Financial Instruments:

1. The financial system deals in financial assets, services, and instruments.
2. There are two categories of financial assets or claims:
3. Primary or direct securities, and
4. Secondary or indirect securities.

Financial claims against real sector units are known as primary or direct securities. Bills, bonds, stocks, debentures, etc. are some examples.

As primary borrowers for the purpose of borrowing money to pay for their deficit expenditure, real sector entities generate them. Financial claims made by financial institutions or intermediaries against themselves in an effort to generate money from the general public are known as secondary or indirect securities.

As an example, consider bank deposits, life insurance contracts, UTI units, IDBI bonds, and so forth. Important financial assets in the Indian economy include, at the moment, bank deposits, post office savings deposits, life insurance policies, provident funds, bonds, bills, dollars, UTI units, nidhis, and chit funds, among others. Regarding their investment, financial instruments are different from one another.

The following are crucial aspects of financial assets: Marketability Reversibility Transferability Cost of transactions Risk, ambiguity, and the maturation phase. As stated before, the financial system is a collection of intricately linked financial markets, instruments, services, and procedures.

A financial system is a collection of institutional structures that enable the transfer of funds from surplus to deficit units. The organized portion of the financial system may be divided into two categories: The disjointed section

The planned section:

The RBI, commercial banks, cooperative banks, NBFIs, foreign banks, etc. are included in it. It is said to be organized since the RBI carefully coordinates all of its components. They compete in their market with non-bank financial organizations like LIC, GIG, UTI, and others. Similar to small businesses, large corporations need banks for financial transactions.In addition to commercial banks, there are cooperative banks.

They have a significant impact on the organized sector. Cooperative credit societies have a three-tier organization, with state cooperative banks at the top, central cooperative banks at the district level, and primary credit societies or urban cooperative banks at the bottom or village level.The RBI controls the way cooperative banking operates. State cooperative banks are a concern for the RBI.

The RBI has jurisdiction over the cooperative banks' operations and size. Although the organized portion of the Indian money market is well advanced, it cannot be compared to the money markets in New York or London. Let's talk about the key players in the Indian stock market.

DISCUSSION

Call Money market

Almost all established money markets have a call money market. Mumbai, Kolkata, and Chennai are the three primary locations for the CM market in India. Mumbai is the most significant CM market among them. Transactions involving borrowing and lending take place in the call money market for a single day. 'Call Loans' is another name for these loans. The next day, they may or might not be renewed. The 'inter-bank' call money market is another name for the CM market. It comprises of Discount and Finance House of India, cooperative banks, and scheduled commercial banks. 'Lenders' in this market include organizations like the UTI, LIC, GIC, and IDBIs. Brokers are crucial in the CM market.

The market for Treasury Bills:

Treasury Bills Market is the name of the market where Treasury Bills are traded. In India, TBs are the Central Government's short-term liabilities. TBs should be issued to cover short-term deficits that a government has as a result of having too much spending relative to its income. In India, the market for Treasury Bills is poorly established. There are no significant holders of TBs other than the RBI. Commercial banks, state governments, and non-bank financing intermediaries like the LIC and UTI are among the other holders of TBs.

Repurchase Market

Repo is a money market product that facilitates lending and borrowing for a brief period of time. In a repo transaction, the holder of the securitized assets sells them to an investor with the promise to buy them back at a later date and at a fixed price.

The market for Commercial Bills:

Trade bills or commercial bills are handled in the commercial bill market, which is a submarket. A bill written by one merchant enterprise on the other is known as a CB. CBs often result from domestic transactions. Due to the widespread use of the cash system in bank financing and the unwillingness of the bigger buyer to commit himself to the payment discipline associated with the commercial bill, the commercial bill market in India is very undeveloped. Therefore, commercial bills serve as a crucial form of credit for banks as well as corporate organizations.

The market for certificates of deposit:

A Certificate of Deposit (CD) is a document that a bank issues to the depository of monies that are deposited with the bank for a certain length of time. CDs are similar to deposits in that they are negotiable and tradeable in the short-term money markets. In order to increase the variety of money market products and provide investors more freedom, CDs have been available since 1989. Commercial banks provide CDs in multiples of Rs. 25 lakhs. Like with government securities, the maturity of CDs ranges from three months to one year. Banks that provide commercial products charge high interest rates on CDs. Since their debut, CDs have been very popular.The commercial paper is a short-term tool used by corporations to raise money. It is a particular kind of unsecured promissory note that the issuer sells to a lender or a security company. The CP was launched in India in January 1990. A listed business that has a working capital of at least Rs. 5 crore and a maturity of between three and six months may issue the CP. Subject to a minimum issue size of Rs. 1 crore, they will be issued in multiples of Rs. 25 lakh. The interest rate on CPs ranges from 11% to 21%. In June 1993, there were Rs. 2,040 crores of funds under CPs. 556 businesses have issued CPs as of today.

Mutual Money Market Funds:

The RBI established money market mutual funds in April 1992. To provide private investors another short-term option, the program had that as its main goal. In November 1995, the RBI approved a number ofeasings with the goal of enhancing the scheme's flexibility. The maximum size for MMMFs that may offer units to corporate entities and others on par with mutual funds is Rs. 50 crores. The scheme's lock-in period is now 15 days. The MMMFs are now obligated to invest the funds they have raised in call money, CDs, CPs, Commercial Bills, TBs, and government securities. Since March 2000, the MMMfs have been placed under the jurisdiction of SEBI rules.

Market for government securities:

The gilt-edged market is the name given to the market for government securities. Government securities are risk-free and are referred to as "gilt-edged" since the government cannot fail on its payment commitments.

Benefits of government securities include:

1. Both refunds and safety are assured.
2. There are two segments of the market for government securities:
3. Market for new issues, and
4. Primary market
5. In the market for government securities, the RBI is crucial. The only dealer in the market for government securities is the RBI.

Unstructured section:

The unorganized market refers to the unorganized sector. It is composed of local bankers and lenders. It is disorganized because the RBI and other authorities do not consistently coordinate the activity of their market. Nidhis, chit funds, local bankers, and moneylenders are the key players in the unorganized money market. They provide loans to potential borrowers who are unable to do so from the institutions that make up the organized portion of the money market.

Finance firms:

Frequently succeed in obtaining a significant portion of their funding via deposits, borrowings, and other revenues. Retailers, wholesalers, artists, and other self-employed persons are loaned money by finance businesses. Finance businesses in the unorganized sector demand very high interest rates between 36 and 48 percent. Savings institutions called Chit Funds don't have a set format. Regular members of the unit's funds subscribe to them on a regular basis.The majority of the chit fund industry is in Kerala and Tamil Nadu. Nidhis are most active in South India. They resemble mutual funds in certain ways since only members are allowed to transact with them. There is virtually little information accessible on the amount of money the Nidhis transact in the loan sector since they operate in an unregulated credit market.

Native American Bankers

Native American bankers are private persons or companies that accept deposits, disburse loans, and otherwise conduct banking business. The RBI does not have any power over the financial operations or transactions, hence they fall within the purview of the unorganized sector of the money market. Similar to moneylenders, native bankers are adaptable, casual in their style, and rapid in their transactions. Their reports are clear and precise. Public deposits

are accepted by indigenous banks for both short- and long-term use. The interest rate at that time is between 3 and 9%. The local bankers often use the following approaches while doing business. lend money using promissory notes with a written demand. The Promissory Notes must include the sureties' attestation if the loan amount is substantial. There is a high interest rate applied in the absence of testimony. Additionally, loans are given against mortgaged lands, homes, or other assets. Native American bankers who employ indigenous trade currencies known as Hundis and discount them in order to give credit. Native bankers have begun to disappear, nevertheless, as contemporary organized banking has expanded and financial activities have become more institutionalized.The components and function of the Indian financial system.Financial institutions, markets, instruments, and services are all different types of financial system aspects that are interconnected and do not compete with one another.

Institutions of finance

Financial institutions, also known as financial intermediaries, are described by Dr. LM. Bhole as "business organizations that act as mobilisers and depositories of savings and as purveyors of credit or finance." They fall within the category of financial institutions. Banks, often known as banking institutions, mobilize money by collecting deposits and disbursing loans to individuals and businesses. Credit "creators" include institutions like the RBI, commercial banks, and cooperative banks.

Non-banking institutions:

Non-banking institutions are able to borrow money from the public directly or indirectly and lend it out, but they cannot provide credit. These people are referred to as "purveyors" of credit. As an example, consider the Insurance Corporation of India, the Unit Trust of India, and the Industrial Development Bank of India.

Intermediaries and non-intermediaries are two additional categories for financial institutions. Investors and savers are connected via financial intermediaries. They both mobilize funds and provide loans. All financial establishments serve as middlemen. Non-banking intermediaries provide funding for certain purposes, industries, and geographical areas. For instance, non-banking entities like LIC, GIC, UTI, and PF channelize depositors' money via a variety of programmes and lend it for investments.

Monetary Markets

Financial markets and institutions support the operation of the financial system. Financial markets are the places where services for financial transactions are offered. They deal with many financial instruments and assets, including cash, checks, bills, and bonds.Primary market is one of many categories for financial markets. Secondary market, tooprimary market: handles brand-new securities and financial claims. Consequently, they are also known as the "New Issues Market." They mobilize saving and provide more capital as a result. Deal with already-issued assets in the secondary market. They don't immediately add to the capital supply. Money and capital markets are additional categories for financial markets. Short-term claims are dealt with in money markets. Long-term claims are dealt with in capital markets. In a third division, financial markets are divided intoregulated market. Unorganized market is also.

Commercial banks, cooperative banks, and the Reserve Bank of India make up the organized money market.Shroffs, local bankers, and money lenders make up the unorganized money market. They fall outside of the scope of organization and management.Banks and non-

banking financial organizations including IDBI, Development Financial organizations, insurance companies, UTI, and the stock market are all part of the organized capital market. Informally run financial institutions and Nidhis funds make up the unorganized capital market.

financial product or service

The financial assets or claims that make up a significant portion of the financial system are known as financial instruments. Deposits with banks, businesses, corporations, and the post office, insurance policies, National Savings Certificates, and Provident Fund, among other things

Pension plans, stock investments, and bonds and other instruments.

Primary Securities are the financial claims made to real savers in order to mobilize deposits, such as government, corporate, and company securities purchased with excess funds from banks and other financial organizations. Banks and other financial entities that issue financial claims against themselves are referred to as issuing "secondary securities." This gives them the ability to produce resources from which they may produce direct money for investing in primary securities.

1. Financial System's Function

The financial system is essential to the economy's operation because it facilitates the flow of funds from depositors to families, businesses, merchants, and governments. It generally hastens the pace of economic expansion. The financial system offers the tools and services necessary for a contemporary expanding economy. The financial system and its tools influence a nation's rate of economic growth. Investment and saving provide the fuel for growth. The economic development is facilitated by the consistent and comprehensive deployment of financial resources. The performance of financial institutions and the tools they employ will improve if a financial system develops in a balanced way. A healthy financial system is built on the basis of macroeconomic stability, improved accounting, and regulatory systems. A financial system's primary goals are to encourage saving and its mobilization. Effective distribution of savings from a social and economic perspective, and Facilitation of economic activities including the exchange of commodities and services and trade. After liberalization and the post-reform period, the financial sector has seen a significant shift in function. Deregulation efforts included removing direct restrictions, liberalizing interest rates and credit distribution, removing limitations on foreign currency and transactions, allowing free admission of new businesses, and expanding the financial system's foundation.

As a result, the financial system creates a connection between depositors and investors, promoting savings and investment in an economy. It effectively distributes resources. The achievement of national economic development is its ultimate objective. The vital function of the financial system is to produce resources and utilize savings for useful purposes. The financial system is responsible for coordinating savers' choices and turning funds into financial assets. The financial system functions as a circuit for converting available funds into investments. As a result, the financial system offers a method for converting resources into assets.

The Financial System's Functions

By offering credit, loans, and other associated services, the financial system facilitates the trade of commodities and services. It makes arrangements for the movement of money across

time and geography and mobilizes financial resources or finances. It offers strategies and tools for controlling risk and uncertainty. It facilitates information generation and decision-making.

Functions:

Exchange of products and services: Transactions may happen via payment, which is made possible by the financial system's support of tools like Hundi, bills of exchange, etc. Therefore, those who are buying and selling products and services want to get bank credit, which enables them to carry out their trade operations more easily and freely. The provision of credit facilities by commercial banks, which aid in the transaction of goods and services, is crucial. The banks also give services to customers in the form of various sorts of credit and generate credit. Promotion of investment and savings: In order to encourage capital development, resources or cash must be transferred from savers to investors. To fulfill the capital requirements of the production units, the financial system's role is to mobilize the money and convert them into financial instruments and assets. As a result, the banks and other financial institutions serve as a conduit between savers and investors by converting resources into investments in the creation of goods and services.The people sell their labor and earn money, which they use to meet their daily needs and set away a portion of their earnings as "savings." This is the mechanism for the transfer of financial resources. This saving serves as a significant source of funding for the production of products and services in the real sector.The task of transferring money from holders of surpluses to borrowers falls on the financial system. This is nothing more than a bank's role in receiving deposits and disbursing funds to borrowers. As a result, the financial system not only facilitates the transfer of money but also encourages saves by giving investors a variety of possibilities for real estate investments.

Risk and Uncertainty Management:

Everyone's future is uncertain. The risk and uncertainty associated with future investments drive the need for risk management. Most consumers decide to invest or save in low-risk products such bank deposits, post office savings certificates, and busy saving certificates. People choose short-term loans because it allows them to manage risks. The financial system, which includes banks and non-bank entities, deals with a variety of assets and offers options for managing risk and uncertainty.

Information generation:

The financial system also produces data on the various lending and borrowing choices available. As a result, both savers and borrowers learn about financial possibilities and learn how to direct investment. The advancements in information technology have broadened the range of investing opportunities in the modern world. Due to electronic communication systems, domestic financial markets are more closely linked to the global market.

Finance and development are connected:

Finance and development's interaction may be seen as a "virtuous circle" between them. Finance is readily available, which promotes economic expansion, which results in financial expansion. Financial institutions encourage saving and investing by increasing the savings rate, which increases savings and allows for investment into profitable ventures. Thus, the growth of human capital coincides with that of the financial sector. Capital was capital market mitigated. Financial markets minimize risks, amplify certainty, and improve investment effectiveness, increasing output.

CONCLUSION

In conclusion, The RBI, commercial banks, NBFCs, and other financial institutions along with other market participants make up the dynamic ecosystem that supports short-term capital movement and liquidity management in the Indian money market. The Indian money market is a key part of the nation's financial system since it has a broad variety of money market products and efficient regulatory frameworks.

Policymakers and market players should maintain the money market's resilience and flexibility by continuously improving laws and encouraging innovation, which will support India's overall financial stability and economic progress. Despite its advantages, the Indian money market confronts a number of difficulties, such as the need for more depth and liquidity, increased instrument diversity, and improved transparency and disclosure norms. The development of a more resilient and effective money market that can accommodate the changing financial demands of the economy will depend on addressing these issues.

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CHAPTER 6

A STUDY ONINDICATORS OF FINANCIAL DEVELOPMENT

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ABSTRACT:

Financial development is a critical aspect of any economy, playing a vital role in fostering economic growth, stability, and prosperity. This paper examines the indicators of financial development that provide insights into the effectiveness, efficiency, and depth of a country's financial system. The study explores various indicators, including the size of the financial sector, the level of financial intermediation, access to financial services, and the development of financial markets and instruments. It also delves into the significance of these indicators in evaluating the overall health and performance of a nation's financial landscape. Understanding the indicators of financial development is crucial for policymakers, investors, and researchers, as it enables informed decision-making, effective policy formulation, and the identification of areas that require further development and enhancement in the financial sector.

KEYWORDS:

Capital Markets, Credit Availability, Economic Growth, Finance, Financial Inclusion.

INTRODUCTION

The function of the financial system in economic growth is clarified by this item. The production theories have examined how money, or capital, influences economic growth via savings and investments in addition to being an input in the production process. Since 1950, the Indian financial system has expanded significantly. The development of our financial system is shown by measures like the finance ratio, financial interrelation ratio, new issue ratio, and intermediation ratio. These ratios aid in determining the business value in addition to measuring a financial system's performance. The Indian financial system has greatly expanded and developed, and it has considerable capacity for saving mobilization and servicing commercial and industrial demands[1], [2].

System of Finance and Economic Development

A nation's financial system is crucial to its economic growth. Only when a nation's national income, savings, investments, and employment all demonstrate growth are these factors conducive to economic progress. A sound financial system permits risk in saving and investing, which helps to increase employment, output, and income. As a result, it may contribute to the nation's planned, all-around economic growth. The Indian financial system provides a broad variety of services that operate in both the money and capital markets via its network of banks and other financial organizations. The fact that the financial system includes a mechanism to assist the production and exchange of goods and services by employing the resources for lending and producing credit is an important component of the financial system. Commercial banks assist in the creation of products and services by providing producers with loans or credit. Credit is then created by financial organizations like banks in anticipation of the mobilization of savings. As a result, the financial system promotes economic growth. Future income will grow as a result of increased investment and saving[3], [4].In a nutshell, the financial system supports economic growth in the following ways:

1. Promoting savings via various investment possibilities for the deposits;
2. Effectively allocating savings.
3. Making trade, commerce, industry, and agriculture easier to achieve in order to achieve economic growth.

Finance and development are connected: 'Virtuous circle' might be used to describe the link between money and development. Finance is readily available, which promotes economic expansion, which then results in financial growth. The levels and variations in FIR show that India's national income increased once the financial system expanded. The institutionalization of investment finance has also increased noticeably, widening the gap between saving and investment[5], [6].

Economy's Different Sectors and the Financial System:

1. The corporate and financial sectors
2. The domestic economy and financial system
3. The financial system and the public or private sector
4. The financial system and external or foreign sector.

Financial system and corporate sector:

Private limited firms, public limited companies, and cooperatives make up the corporate sector. These organizations are quite large-scale businesses involved in manufacturing, commerce, and financial services. This industry needs both short-term and long-term capital, and the units within it struggle to get money for investments[7], [8]. The commercial banks and new issues market provide financing to the private sector entities. They must also adhere to other financial practices, such as equity issuance, public deposits, debt financing or borrowing, etc. financial system and the household sector. Individuals, their families, and small businesses in commerce, manufacturing, and agriculture make up the household sector. Out of their excess income, they save both big and little amounts. Mobilizing national savings is the primary role of the financial system.Savings in the household sector include two parts:

Both financial and physical assets, including as bank and non-bank deposits, LIC insurance, units of UTI, shares, and debentures, are considered assets. An economy cannot sustain savings at a constant pace. Economic circumstances, interest rates, income levels, savings goals, governmental policies, tax rates, etc. all have an impact on it. The emerging nations exhibit their reliance on the flow of money from outside by creating a saving-investment gap when it comes to the mobilization of savings to satisfy investment needs. In contrast to the deficit created by private corporations, the government sector, and the public sector, the household sector creates a surplus, or net saving, across all sectors. In regards to their development and expansion, the household sector saving and the financial system are intertwined.the financial system and the public or private sector.

In emerging nations, the government is crucial to economic growth. Public sector of the government comprises government firms[9], [10]. The government is required to spend money on a variety of things, including defense, education, programs to reduce poverty, health care, roads, and communications. The government does not receive enough money from its sources of revenue, such as taxes, levies, and fees, to cover its expenses. The RBI, UTI, IDBI, GIC, LIC, and other institutions as well as external sources like borrowing from other countries are additional sources of revenue. The debt market in India is growing increasingly significant. It would make it possible for banks and other financial institutions to meet the governmental sector's financial demands. OMO would be followed by RBI. The debt market would promote the creation of new risk management products that would allow

market players to control interest rate risk. Thus, the debt market meets the need for governmental spending on housing, infrastructure, etc.

The external or foreign industry and financial system have seen a surge in foreign investment during the last several years. The following three methods are used for foreign investment:

1. MNC and NRI investments
2. Foreign support or aid
3. Support from global financial institutions.

The role of the external sector in gaining access to finance is increased since both the public and private sectors are unable to raise the cash needed for investment. The cost of maintaining and repaying deposits from non-resident Indians and loans from foreign organizations is substantial. Financial products such as convertible bonds, American depository receipts, and global depository receipts were favored by the policies of liberalization. Additionally, access to investing in India has been granted to foreign institutional investors. Foreign Direct Investment, which accounts for 40.22% of all foreign investments in 1996–1997 and is valued at $ 2,587 million, has surpassed FLLs' net portfolio investment. The public and private sectors are considered "deficit" sectors because they result in a saving-investment imbalance, which prevents them from raising money for their own investments.

The household sector is a net "surplus" sector that provides financial assets with its savings as the main source of capital for the country and aids in closing the gap between saving and investment. Debt- and non-debt-creating foreign capital inflows may help close this imbalance. The Indian Financial System has advanced significantly in terms of innovation, variety, modernity, and technology. The efficiency of a financial system affects a nation's economic growth. In emerging or less developed nations like India, where finance is a source component, it is essential for economic growth. a well-developed financial system with the right institutions in place to mobilize savings and facilitate their conversion to financial assets. The remarkable banks and NBFC that make up the Indian Financial System provide a broad variety of goods and services in both the capital and money markets. As a result, it plays a significant role in India's economic growth process. Finance Ratio, Financial Institution Ratio, and Intermediation Ratio are all indices of financial development that have all shown considerable increases.

Reforms in the Financial Sector

Programs for structural adjustment and stabilization were launched under the New Economic Policy. The Indian banking industry has seen significant changes as a result of it. A committee headed by M. Narsimham was established by the Indian government in August 1971, immediately after the launch of NEP, to look at the Indian Financial System. The committee required to discuss the Indian financial system's structure, organization, operations, and processes. In 1991, the committee delivered its report in a timely manner. A second committee on banking sector reforms was established in 1998 and M. Narismham served as its head.

This committee's report was presented in April of that year. The foundation of committees was the idea that because the money in the banks comes from the general public, it should be utilized in a way that maximizes benefits for the depositors. The banking industry and the Indian financial system have benefited from the reformers' efforts to make them robust and competitive.

1991–1992 Narismham Committee Report

Under the leadership of M. Narsimham, a high-level committee was established in 1991 to review many areas of the financial system's structure, organization, activities, and processes. The group's report was delivered in November of that year. The Committee highlighted the shortcomings of the Indian Financial System as well as its successes and advancements. It said that during the New Industrial Policy era of 1991, the financial system needed to be more efficient and competitive to satisfy the demands of the real economy. The committee concentrated on ensuring that the financial services operate on the basis of operational flexibility and functional autonomy to increase efficiency, productivity, and profitability while making its recommendations for financial sector reforms.

DISCUSSION

Operational Flexibility and Functional Autonomy

The Narsimham Committee contends that the financial services sector should run independently and with operational independence. Bank managements should be trusted to make the best decisions about internal structure. Similar to this, for functional autonomy, each bank should be allowed to hire its own officers rather than using a centralized hiring process.

Credit limit reduction for the priority sector: The credit limit for the priority sector must be decreased from 40% to 10%. Similar to this, the term "priority sector" has to be revised to include cottage, village, and small company enterprises as well as small and marginal farmers. A phase-out of the directed credit scheme was also suggested by the committee.

Deregulation of interest rates: The committee discovered that the stiff and complicated structure of interest rates. Deregulation of interest rates is thus necessary. Concessional rates need to be eliminated gradually.

Elimination of capital insufficiency: Capital insufficiency affects Indian banks. It should be eliminated during the next three years, the committee said.

Loss Provisioning and Income Accounting

Income production has suffered as a result of the loan portfolio's declining quality. Therefore, the committee has made the following recommendation: Bank assets should be assessed using their accurate valuations. The'realisation' approach of accounting should be used by banks and financial institutions. For non-Performing Assets, no revenue should be shown in the accounts. If interest on an asset is past due for a period longer than 180 days, the asset should be deemed non-performing.

Special Tribunals

In order to hasten the recovery process and ensure that the debts owed to the lending institutions are paid in a timely manner, Special Tribunals will be established.The committee suggested that an Asset Reconstruction Fund be formed, which would purchase questionable loans at a discount from banks and other institutions. The government. of India intends to lend money to FIs and banks in this respect.

Erosion of Profitability on the Expenditure Side: Due to massive branch expansion, overstaffing, etc., the committee recommended eliminating branch licensing, leaving branch opening and closing to the commercial judgment of banks, evolving policies for "right sizing," using a computerized system, and abolishing branch licensing. The committee

recommended that new banks in the private sector be encouraged and that there should be no additional nationalization of banks. Structure of Rural Credit: The committee suggested that each Public Sector Bank acquire control of a Rural Bank in order to increase the profitability of Regional Rural Banks. RRBs' interest rate structures have to be comparable to those of commercial banks.The committee was against the RBI's dual regulation of the banking industry with the Ministry of Finance's Banking Division. The committee suggested that the RBI be designated as the key regulatory body. Additionally, a new entity will be established under the RBI to oversee banks and DFIs.

Foreign Banks

The committee suggested allowing foreign banks in India. International banks and Indian banks should collaborate. For the operation of new institutions such merchant banks, mutual funds, and leasing companies, it is also necessary to establish prudential rules and guidelines.

Report of the Narsimham Committee, 1998

On April 23, 1998, the Second Narsimham Committee's report on banking sector reforms was delivered. The second Narisimhan Committee made the following recommendations:

Banking system with three tiers:

The committee suggested making a concerted effort to create a system of two or three big Indian banks with a global scope. There should be eight to ten national banks on the second tier. The last surviving regional or local banks should be at the third tier. This is for complete convertibility and deeper financial system integration.

Handling of Weak Banks Differently:

The issues with weak banks should be dealt with individually. These banks may be shut down if required. In order to address the massive backlog of BPAs, which has negatively impacted the efficiency and profitability of banks, certain steps will be made to address the non-performing assets (NPAs) of nationalized banks, which are regarded as bad debts.

Combining DFIs:

The committee made further recommendations about how development financial institutions operate in comparison to commercial banks. The committee then advised that DFIs in India unite.

Flexibility in Operations for Public Sector Banks:

The group suggested giving public sector banks some operational latitude. It advocates giving the bank management functional autonomy and establishing responsibility for their underperformance.

New Guidelines from BIS:

The committee suggested that the Bank for International Settlement's new basic principles be followed. Similar to this, a suitable legal structure is required to safeguard secured creditors' interests, particularly in bankruptcy situations.

Examining sick industrial facilities

It is required to assess the ill industrial units in accordance with the banking modifications. Therefore, the committee advises that their performance be evaluated.

Banking Boards' Depoliticization:

The group has advocated for the complete depoliticization of chairman and banking board appointments. The committee examined how partisanship had an impact on the selection of key bank executives. With regard to the appointment of non-official personnel, nothing of the kind occurred.

Enhancing The Banks' Inherent Strength

According to the committee, the country's second phase of financial and banking sector reforms must focus on boosting banks' natural strengths and reviewing the system's structure while taking institutional and technical factors into consideration. After economic reforms were implemented in 1991, the Indian economic system demanded a suitable environment for the banking and financial sectors. The financial sector, which is the foundation of the economy, needs to be given an international character in order to reap the maximum benefits from globalization. The primary goal of financial sector reforms is to increase resource allocation responsibility and quicken the pace of economic growth. Reforms in both the banking and non-banking industries focused on building a deregulated environment and attempting to enhance the prudential standards and regulatory structure. The 1991 and 1998 Narsimham Committee proposals were quite beneficial. The committee's 1991 report identified issues with profitability, efficiency, loan quality, rural credit structure, and financial services. Recommendations such as capital sufficiency, standards, financial autonomy, CRR reduction, operational flexibility, and deregulation of interest rates are used to address these issues. The Second Narsimham Committee, which was established in 1998, put out suggestions on the banking sector, DFI mergers, BIS principles, NPA reforms, operational flexibility, and other topics.

Monetary policy and central banks

The central bank of a nation is crucial to that nation's economic growth. The major job of a central bank, especially in developing nations, is to make it easier for financial institutions to operate by fostering and upholding a favorable environment for investment and growth. Similar to this, financial laws are essential to preserving public trust and confidence in banks.The government, the Reserve Bank of India, the Securities and Exchange Board of India, the Insurance Regulation Authority, IDBI, SIDBI, and other significant authorities are in charge of financial regulation in India.The Reserve Bank of India is the main financial and monetary institution in India. Since its founding, it has served as the apex level entity directing, regulating, and advancing Indian finance. In accordance with the RBI Act of 1934, it began operating on April 1, 1935. The RBI was founded in 1773, when Warren Hastings saw the need of a national central bank. the pyramidal diagram that is shown below. The RBI was previously established as a shareholder's bank with a share capital of Rs. 5 crores. According to the Reserve Bank of India Act, 1934, the RBI's primary function is "to regulate the issue of bank notes and keeping of reserves with a view to securing monetary stability in India and generally to operate the currency and credit system of the country to its advantage." The RBI was nationalized in 1949. The Central Bank received the whole shares.

Central Bank's goals

1. To keep the nation's currency valued within.
2. Maintaining the currency's external value
3. In order to create pricing stability
4. To encourage economic expansion
5. To assist in preserving the nation's revenue, productivity, and employment.

These goals are essentially the same for all nations in the globe. Another key goal of the RBI in India is to operate well or preserve financial stability while avoiding political interference.

Activities of the RBI

The central bank of our nation is the Reserve Bank of India. It is India's top financial institution. It directs, oversees, regulates, manages, and supports India's financial sector. It began operating on April 1st, 1935. Important developments occurred in India during this time. On August 15, 1947, India attained independence, and the government made the decision to start the process of planned economic growth. A state-owned central bank was seen to be better suited to meet the needs of economic growth. The RBI was subsequently nationalized on January 1, 1949.

Currency notes issuance

Since its founding, the RBI has had the only authority to issue currency notes other than notes worth one rupee, coins, and coins with lesser values. The Indian government issues one-rupee bills and coins, which are then circulated by the RBI. The proportionate reserve scheme used in the original Act was eventually superseded with the minimum reserve system for note issuance. The RBI Act of 1957 stipulates that a minimum reserve of Rs. 200 crore must be retained.

Government-Employed Banker:

The central and state governments use the RBI as a lender. It offers the government all varieties of banking services, including accepting deposits, making payments, allowing check withdrawals, transferring money, and managing the nation's debt. The RBI advises the government because it has solid expertise of the financial market.

Bank for bankers:

The RBI Act of 1934 and the Banking Regulation Act of 1949 provide the RBI the authority to regulate the commercial banking industry. According to this, all banks are obligated to keep a certain proportion of their deposits with the RBI. All scheduled banks are required by law to keep a minimum amount of cash on hand with the RBI to cover their demand and time commitments. Scheduled banks and state cooperative banks get financial support from the RBI in the form of loans secured by securities.

The RBI also oversees other aspects of banking regulation, including bank licensing, branch growth, asset management, mergers, and liquidity.

Credit Control Officer:

Credit control is seen as the central bank's primary duty. Like every other central bank, the RBI uses both quantitative and qualitative approaches to regulate credit. Quantitative techniques include open market operations and bank rate policy. Ratio of cash reserves. Margin restrictions, moral persuasion, credit rationing, direct intervention, etc. are examples of qualitative approaches. The Statutory Liquidity Ratio and CRR have been used by the RBI as possible tools for credit management. Bank lending volume is altered using the bank rate. For qualitative credit control, the RBI also employs Selective Credit Control techniques.

Management and control of exchanges:

Maintaining the stability of the rupee's external value is one of the RBI's key duties. The nation's foreign currency reserves are kept safe by the RBI. The Foreign currency Regulation Act was established in 1947, and as a result, the RBI's role in managing and controlling

foreign currency became crucial. As a result, it must manage foreign exchange, choose an exchange rate system, and set the exchange rate between the rupee and other currencies. control the foreign currency reserves and communicate with the IMF, World Bank, Asian Clearing Union, Sterling region, and other international monetary agencies.

Credit management

Credit control is seen as the key role of a nation's central bank. The Reserve Bank uses quantitative and qualitative techniques of credit control to manage and control the amount and direction of loans. The two quantitative techniques are the credit reserve ratio and the bank rate policy. Moral persuasion, credit restriction, margin requirements, direct action, etc. are examples of qualitative approaches.

Finance for Agriculture:

An exclusive duty of the RBI is to fund the agricultural industry. This encourages India's agricultural growth. On July 12, 1982, the National Bank for Agriculture and Rural Development was established, taking over many of the responsibilities of the RBI's Agricultural Credit division.

Promotional and Development Tasks:

The duties of the RBI extend beyond credit control and other routine tasks to include a wider range of development and promotion. In order to promote economic growth, the RBI's promotional activities have contributed to the mobilization of savings and the steering of credit flows to the intended purposes. The RBI encourages banking practices and services in semi-urban and rural communities.

The RBI has prioritized the growth of institutional lending, establishing the Agricultural Refinance and Development Corporation in 1963 and NABARD in 1982. The Industrial Development Bank of India, State Financial Corporations, and Industrial Finance Corporation-of-India are only a few examples of the industrial finance organizations that the RBI is in charge of.The goals of monetary policy are: A larger macroeconomic strategy, which also encompasses the government's trade and fiscal policies, incorporates monetary policy. As a result, the macroeconomic goals of the nation also serve as the goals of monetary policy.

Financial Independence:

In the monetary system, money should be a non-active or neutral element. It shouldn't be permitted to affect the actual economic considerations in any way. Professor Hayek has declared this goal. Money shouldn't be permitted to have any impact on the amount of revenue, production, or employment, in his opinion. It should only be permitted to serve as a "Medium of Exchange." The level of prices shouldn't be influenced by money. Money supply should be permitted to fluctuate in response to changing money demand. However, the amount of money must be modified in a way that maintains a constant effective supply. Money should be printed in less amount when circulation speed picks up. Therefore, money ought to be a neutral component of the monetary system. It shouldn't be permitted to affect actual economic considerations in any way.

Economic stability or price stability

Price stability suggests that monetary policy should focus on preventing price swings or volatility. Price changes may cause the economy to either experience inflation or deflation. While rich nations struggle with deflation, developing economies mostly deal with inflation.

The economic inflationary tendencies are produced by the development process itself. It is possible for the economy to experience hyperinflation or depression if urgent action is not taken to curb inflation or deflation. Therefore, the monetary policy's goal is to keep prices stable in the economy while also managing inflation. The concept of stability has a broader connotation in the context of a developed nation. It entails avoiding business cyclicality and swings. To guarantee full employment, the economic cycle's two primary periods of depression and recession are avoided. Therefore, it is anticipated that the monetary policy would implement appropriate steps to stabilize the industry.

Economic Expansion

The main goal of monetary policy in emerging markets should be to achieve this. But unlike fiscal policy, which may directly affect investment spending in the economy, monetary policy is not well suited to achieve this goal. It works by giving incentives via changes in interest rates, the ease of obtaining loans, etc.

Justice for all:

Many economists have recently brought up social justice as a goal of monetary policy. This is one of the nation's desired macroeconomic objectives. This goal may be achieved by monetary policy's specialized credit control tools. Consider the use of selective credit control to provide small and marginal farmers with easy loans. Similar to this, unsecured modest loans may be given to those in need in order to help them begin productive activities in accordance with monetary policy. Due to this, more people may become self-employed and find work. As a result, it is possible to reduce the wealth gap and achieve social fairness via economic growth.

Complete Employment

In developed nations, the goal of full employment is highly popular. The complete use of all resources within an economy is implied by full employment. Consequently, it may decrease unemployment and increase work prospects. Monetary policy may achieve this goal by promoting economic investment. This goal may be attained by using monetary policies like the bank rate policy and selective credit control tools.

CONCLUSION

In conclusion, in order to improve economic growth, stability, and inclusion, policymakers and stakeholders must closely monitor and comprehend financial development indicators. A well-designed financial system that takes into account the various requirements of people, companies, and the larger economy may act as a catalyst for sustained growth and prosperity. Countries may execute efficient financial reforms, make well-informed policy choices, and create robust and healthy financial systems that are advantageous to society as a whole by using these indicators as guiding benchmarks. A balanced strategy is needed to promote financial growth, one that takes into account both the need of expanding access to financial services and the significance of preserving financial stability. In order to reduce systemic risks, policymakers must concentrate on regulatory frameworks that encourage innovation, competition, and consumer protection.

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CHAPTER 7

A BRIEF DISCUSSION ON MONETARY POLICY OF THE RBI

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ABSTRACT:

The monetary policy of the Reserve Bank of India (RBI) plays a critical role in influencing economic growth, price stability, and financial stability in the country. This paper examines the key elements of the RBI's monetary policy, including the objectives, tools, and strategies employed by the central bank to achieve its goals. It explores the significance of interest rates, reserve requirements, open market operations, and other monetary instruments in regulating money supply and credit conditions. Additionally, the study analyzes the challenges faced by the RBI in formulating and implementing monetary policy in a dynamic and evolving economic landscape. Understanding the intricacies of the RBI's monetary policy is essential for policymakers, businesses, and investors, as it provides insights into the central bank's efforts to maintain a conducive economic environment for sustainable growth and financial stability.

KEYWORDS:

Cash Reserve, Consumer, Credit Policy, Discount Rate, Inflation Targeting, Interest Rates.

INTRODUCTION

The term "monetary policy" refers to the methods of monetary management used by the nation's central bank to achieve certain economic goals.In India, the primary goals of monetary policy are:

1. To achieve economic progress while maintaining economic or price stability [1], [2].
2. To support financial and monetary organizations.
3. To achieve social justice and equality.

In order to achieve economic goals, a central bank must retain control over the supply of money or credit. This is known as monetary policy. However, in less developed nations, monetary policy goes beyond just regulating the money or credit supply. The RBI's role in an emerging market like India goes beyond credit limitation to include monitoring the ongoing expansion of credit and the money supply to promote commerce and industrial growth. Financial policy must also monitor credit issued for wasteful purposes[3], [4].Following were the goals of monetary policy throughout the planning era.

1. To encourage saving,
2. To mobilize funds for capital development and to boost investment levels,
3. To foster an environment conducive to investment in order to achieve economic goals,
4. To fund economic sectors such as agriculture, industry, trade, and commerce, among others.
5. To keep inflation in control and preserve price stability.

Therefore, India's monetary policy has additional goals outside only controlling the money supply, such as maintaining price stability and promoting economic development. The RBI is the only entity with the authority to print currency notes, ensuring total control over the flow of credit and money. The French monetary system, which uses legal tender money as the

medium of commerce, is similar to the nature of the Indian monetary system. The overall money supply in India was Rs.4,54,490 crore on January 10, 2003, and there were Rs.12,34,596 crore in time deposits. Our nation's monetary policy has had two goals in mind. To satisfy their credit needs, it must promote the flow of a sufficient amount of bank credit to industry, agriculture, and commerce. Additionally, it has carefully chosen tools that provide credit to the less powerful members of society and the underserved areas of the nation. In addition, it must prevent excessive credit growth and make sure that credit is not being used for bad things in order to control inflationary pressures[5], [6].

Tools for Monetary Policy

Quantitative techniques:

The amount of credit or the size of the money supply in the economy is controlled by quantitative techniques of credit regulation. These techniques include the following:

Open Market Activities:

The sale and purchase of government securities are referred to as OMO. In industrialized nations like the USA and UK, this credit control strategy is commonly employed. The RBI has the ability to influence the reserve position of banks as well as the volume and cost of bank lending by making purchases and sales of government securities. Government securities that it may acquire or sell are not limited in terms of number or maturity[7], [8]. With the use of this tool, the RBI is able to affect the commercial banks' reserve positions and, therefore, their ability to provide credit. The RBI ought to have relied more heavily on this strategy in India, where the institutional framework is typically suitable for open market operations. The RBI trades in the market regularly, buying and selling government securities in switch operations; it often does not buy them with cash. The transactions with OMOs are limited to institutional investors in India since they are the only ones that own government securities, including commercial banks, IDBI, NABARD, insurance firms, etc. Additionally, the fact that OMO is primarily employed for debt management undercuts OMO's efficacy. Similar to this, the market for government assets is neither diversified or well-organized, and the interest rates are very low. Therefore, OMOs are now less significant.

OMO was very sometimes used before World War II, but subsequently, the RBI used it more often to stabilize gilt-edged markets and satisfy defense requirements. The usage of this approach has been steadily rising from 1951–1952, rising from Rs. 116 crores to Rs. 10,572 crores in 1991–1992 to Rs. 53,780 crores in 2002–2003. OMOs have therefore assisted in managing the flow of credit to the private sector during this time[9], [10].

Policy of the Bank Rate

The cost and availability of refinancing are controlled using this method, and the quantity of credit given to banks and other financial organizations is altered. The discount rate on advances from other banks and commercial banks is known as the bank rate. The RBI has the authority to use this kind of credit management. The following factors determine how well the BRP works:

Commercial banks shouldn't refuse the RBI's rediscounting services. Banks don't have any extra cash on hand to cover deposits, therefore if depositors make demands, they should be forced to rediscount notes from the central bank. Banks are required to keep a certain amount of credit instruments to avoid having them rediscounted by the central bank. The bank rate was 3% up until 1951, which led to a significant increase of credit and a deficit in the Balance of Payments. Bank Rate was increased to 4.5% in 1964 and lowered to 5% in 1968.

It was increased to 11% in 1991 and then maintained at 12% the following year. This was thought to be required in order to reduce inflationary pressure. The RBI has made actions to tighten the Bank rate policy since the advent of fresh economic reforms in 1991. As a result, the bank rate was reduced to 10% in 1998 and 6% in 2003.

Cash Reserve Ratio (CRR): The CRR is a useful tool for monetary policy. According to the RBI Act of 1962, the RBI has the authority to set the CRR for commercial banks' total demand and time deposits in the range of 3% to 15%. The CRR was increased from 10% to 15% in the late 1980s. However, the Narsimham Committee report did not support CRR as a tool to combat inflation since it had a negative impact on bank profitability and compelled them to charge high rates of interest for loans from commercial banks. Government thus had to 10% cut GRR over a four-year period. In June 2003, the final decrease was brought down to 4.5%.

The Banking Regulation Act of 1962 mandates that banks maintain a 25% Statutory Liquidity Ratio (SLR) against their net demand and time deposits. The Act also gives the RBI the authority to increase SLR to 40% in order to manage liquidity. SLR aims to maintain the solvency of the banks, limit the growth of bank lending, and increase bank investments in government securities. SLR increased to 38.5% in 1990 and stayed there until January 1993. Narshimham Committee claims that high SLR is undesirable since it turns into a tool in the hands of the state and federal governments for resource mobilization. SLR was therefore cut in half between 1994 and 1996, to 25%. As a result, the implementation of the SLR decrease as part of the banking sector reform was effective.

Selective Credit Control or Qualitative Methods:

The regulation of credit for certain objectives is often accomplished by qualitative approaches or selective credit management. The application of selective credit management may stop the abuse of borrowings in emerging nations. Additionally, it may stop speculative stockpiling of necessities and restrain unjustified price increases.

SCC is used by the RBI in three ways:

1. Fixing the required margin.
2. Establishing distinct minimum lending rates.
3. Setting a cap on credit flow amounts.

The RBI has mostly relied on the three SCC procedures mentioned above during the last four and a half decades. In addition to these actions, the RBI may instruct the banks or a specific bank as to whether or not loans should be granted. Margin requirements are used to prevent the hoarding of necessities. The commodities that SCC covered were cereal grains, oilseeds, sugar, gur, vegetable oil, and cotton. In general, the interest rate on loans secured by these commodities was maintained higher than that on loans secured by assets not protected by the SCC. A kind of selective credit control was also used in the 1965 introduction of the Credit Authorization Scheme. In accordance with this, the RBI regulates the credit extended to certain significant debtors. However, as part of changes to the banking system, this plan was discontinued.

Fixing credit standards:

Since the 1970s, the RBI has been giving banks important guidelines and instructions on how to fix flaws in the banking system like under-using credit, sanctioning excessive credit or overfinancing, relying too heavily on the cash credit system, and industrial units stockpiling too much inventory.

Credit planning:

It was a result of planning for the economy. The RBI implemented credit planning with the intention of regulating credit for desired purposes and directing credit flows to desired sectors and localities. As a result, credit quality and allocation were controlled to achieve desired outcomes.

Moral persuasion:

This is another crucial credit control method. This takes the form of sending letters to the banks or trying to convince them to abide by the RBI's rules or monetary policy. The RBI first encouraged commercial banks to take caution while making lending for speculative reasons in a letter that was delivered to them in 1949. The nationalization of 14 major commercial banks in 1969 gave rise to the effectiveness of the moral persuasion strategy. Additionally, the RBI has been providing guidance addressing the flaws in the banks.

DISCUSSION

Evaluation of Monetary Policy of the RBI

The Reserve Bank of India, which is primarily focused on monetary issues, may achieve stability, growth, and social justice via the employment of its monetary tools. Economic growth and inflation have been major concerns for the monetary policy. The policy's other worries have related to how credit is distributed among various industries and to the population's poorer segments. Two sets of goals have been pursued since 1951.

Increase in currency:

It aimed to accomplish the dual goals of addressing the demands of commerce and industry while also containing inflationary pressures in the economy by controlling the expansion of the money supply.

Sectoral Development of funds

The RBI has decided how much money would go to each industry and what interest rates will be. The priority sectors, food grains, key industries (coal, iron and steel, engineering, etc.), poorer segments of the population, and priority sectors have all received particular attention. Inflation management has grown in importance as a policy priority in the 1990s. To slow the rapidly expanding money supply, the policy's main focus has been restraint. The goal has been to get inflation down to one percent. The growth of finances among sectors including agriculture, small-scale industry, public distribution system, and export has been one of the policy's other major concerns.

RBI's use of Financial Instruments

The Bank Rate or Discount Rate, which is the rate at which the RBI lends to the banking system, has been one of the main tools used by the RBI. By changing this rate, the RBI can influence the long-term rates in the money market, the long-term rates in the money market, and the level of economic activity in the economy. Additionally, it affects how much money moves internationally; higher rates encourage capital inflows, and vice versa. The open market operations are another crucial tool that is now being used to restrict the expansion of the money supply because of the quickly expanding foreign currency assets. Government securities are being bought and sold in the operation. The RBI reduces the number of resources available to the banks for lending by taking some of the deposit resources from the banking sector via the sale of securities. When the RBI acquires securities on the open

market, the reverse takes place. As a consequence, the selling banks' stock of securities decreases and their cash balance increases. The Cash Reserve Ratio has also been extensively utilized as a tool to influence the money supply. The government has long utilized a higher percentage, called the Statutory Liquidity percentage, to obtain cash in exchange for assets bearing low interest rates.

Performance of the RBI's Monetary Policy

The monetary policy has had some degree of success. The debate that follows will emphasize its successes and shortcomings. In terms of the priority sectors, monetary policy has been effective in addressing the needs of the nation's economic development; for example, the shortfall from the aim of 40% of total bank credit has not been particularly significant. Similar to that, the funding of a number of significant development programs for the population's poorer segments has been mostly adequate. The success of the monetary policy extends even to the management of inflation.

Monetary Policy Errors

The growth of the money supply has produced the most undesirable results. This has been the situation over the whole protracted planning process. Money has grown at a pace that has been far higher than the growth of actual goods. This has contributed significantly to the sharp increase in prices, which has caused significant harm to the economy and the standard of life for most of the period. The illicit market, speculation, and other ills were also born from it. In a similar vein, the allocation of finances between urban and rural areas, as well as between developed and less developed regions, is not adequate. When one contrasts agricultural and small industry with big organized industry and the service sector, one sees more acute disparities in credit allocation. For its credit requirements, agriculture continues to be largely reliant on moneylenders.

Limitations of the RBI's monetary policy:

The undeveloped nature of the economy is to blame for the majority of the monetary policy's constraints. Let's go through these restrictions in more depth.

Limited application of the policy:

It is important to remember that not every evil can be fought with monetary policy. Every economic issue must be approached from all directions, including the financial one. It must be emphasized that monetary policy can only, at most, have a little impact on the demand for commodities, even in cases of inflation when money seems to be a big driver. A far more extensive policy profile is required for the efficient use of monetary policy to combat inflation.

Currency is Dominant

Because currency makes up a major share of the money supply, banks must deal with the issue of big currency outflows whenever they generate credit. People prefer to utilize cash over checks because it is habit and customary and because relevant institutions are few and outdated. This indicates that a significant part of money often percolates through the economy instead of depositing back into the banking system. This limits the banking system's ability to raise reserves in order to generate new loans. However, it should be highlighted that the monetary policy is becoming more effective.A further impediment to India's predicament is the underdeveloped money market, which restricts coverage and complicates the implementation of monetary policy. The RBI, the State Bank, foreign banks, cooperative

banks, etc. make up the organized portion of the money market. The unstructured portion of the money market is made up of local banks, money lenders, etc. These sectors' connections are not very well established. With the continued development of the organized market and an increase in the number of indigenous bankers collaborating with cutting-edge organizations like the Reserve Bank, things are getting better in this area as well.

Existence of black money

The widespread use of money in the illicit market poses a significant barrier to the effective operation of monetary policy. The actions in this market are not publicly disclosed, and the demand for and supply of money are not maintained to the RBI's satisfaction. This indicates that a significant portion of the money economy continues to exist beyond the scope of the RBI's monetary policy.

Because the RBI was unable to take an independent stance in monetary issues, the work of monetary policy in India was rendered much more difficult. For instance, since the majority of interest rates are set or controlled and unconnected to one another, the instruments' use is still limited to financing fiscal deficits. And to reduce the expense of government, this is being done at low administered rates of interest.

Recent Significant Changes to the RBI's Monetary Policy:

1. Giving banks more operational flexibility.
2. Integration of the FX market, the money market, and the market for government securities.
3. The Indian Financial System has made the market for government securities a significant component.
4. Reforms to the fiscal and monetary systems via a deal between the RBI and the Indian government.
5. Interest rate structure deregulation and simplicity.

An evaluation of the RBI's monetary policy

India's monetary policy was developed in the framework of economic planning, with the primary goal of accelerating the nation's development. According to C. Rangarajan, the monetary policy was influenced by three factors: the fiscal policy, the need to manage the inflationary situation, and the need to respond to the monetary policy. The monetary authorities should be more directly involved in determining how much credit is given to the private sector. The decrease of CRR, SLR, and Bank Rate since the implementation of economic reforms in 1991 strongly suggests that the monetary policy has extended credit for industrial growth and price stability.

The Central Bank fulfills two crucial tasks, namely

i) depositing funds and lending during times of need. and (ii) loans to priority sectors.

The purpose of the credit Bank has, however, altered with time. The central bank in emerging nations must serve as both a regulatory and a promotional institution. The RBI has made a lot of moves to improve the regulatory and promotional elements of banking. It has also preserved and assured flexibility to adapt to the scenario at hand. The efficiency of the financial sector as a whole has also required work.

The Central Bank employs both quantitative and qualitative tools to carry out its dual duties of promotion and regulation. The main goals of the RBI's monetary policy are as follows:

i) Price stability.
ii) An increase in bank credit.
iii) Investment promotion.
iv) Equitable credit allocations
v) Activities including the promotion of specialists and the purchase of food.

The RBI uses both quantitative methods of credit regulation, such as open market transactions and the bank rate, and qualitative methods, such as moral persuasion. The macro-level management of finance is the focus of the monetary policy changes. The new Liquidity Adjustment Facility is used in conjunction with the existing monetary policy tools. Financial markets' liberalization, growth, and integration are to blame for this.

CONCLUSION

In conclusion, the objectives of the RBI's monetary policy are price stability, sustainable growth, and financial stability. It is a dynamic and ever-evolving framework. The central bank strives to react effectively to shifting economic circumstances while upholding its basic goals by deploying a variety of monetary policy instruments and tactics. Forging a positive economic climate, creating investor confidence, and safeguarding the general health of the Indian economy all depend on a well-calibrated and aggressive monetary policy. To make wise judgments and successfully navigate the economic environment, policymakers, firms, and investors must be aware of the RBI's monetary policy measures and their possible ramifications.

Additionally, new financial market inventions and developments provide additional difficulties for the implementation of monetary policy. In order to ensure stability and efficacy, the central bank must be careful in keeping track of these developments.

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CHAPTER 8

EXPLORES THE ESSENTIAL ASPECTS OF COMMERCIAL BANKING

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ABSTRACT:

Commercial banking is a fundamental component of the financial system, providing a wide range of financial services to individuals, businesses, and governments. This paper explores the essential aspects of commercial banking, including its functions, role in the economy, and the various products and services offered by commercial banks. It delves into the significance of deposits, loans, and credit creation, as well as the regulatory framework that governs commercial banking activities. The study also examines the challenges and opportunities facing commercial banks in an ever-evolving financial landscape. Understanding commercial banking is crucial for policymakers, investors, and customers, as it enables informed decision-making, effective risk management, and the promotion of a stable and efficient financial system.

KEYWORDS:

Assets, Capital, Central Bank, Commercial Banks, Credit Analysis, Deposit Accounts.

INTRODUCTION

Commercial banks are crucial to the process of economic growth, as economists have constantly emphasized. The simplest and oldest kind of banking is this. They are the pillars on which a country's financial system depends. They increase a nation's money supply while being under the direction and control of the central bank. The lending and investment operations of commercial banks support the economic process of production, distribution, and consumption. The nature and focus of banking as an institution have evolved throughout time. In India, commercial banks are quite rare. This has been shown through the organization's development, programs, and activities in India[1], [2].

List of Commercial Bank Definitions

Banking is defined as "accepting for the purpose of lending or investing money from the public, repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise" under the Banking Regulation Act of 1949.It is a facility for the safekeeping of money received from or on behalf of its client, according to the Oxford Dictionary. It carries out the fundamental duties of taking deposits and disbursing loans to its clients. A banker is a trader in both his own and other people's debts, according to Crowther. the debts of others in return for his own, making money in the process. Therefore, a commercial bank is a kind of financial intermediary that takes public deposits in exchange for loans with the intention of making a profit. Now let's talk about the numerous roles that commercial banks have played recently. Banks contribute to a nation's economic development by carrying out these duties[3], [4].

Business Banking Since Independence, commercial banks have mostly been businesses with the aim of maximizing profits. The primary distinction between commercial banks and other corporate concerns is that Indian banks also have duties related to social welfare, social fairness, and regional balance. The profitability and liquidity of the banks must be properly

balanced. Commercial banks are required to maintain a portion of their deposits as cash reserves, or liquid cash[5], [6].

Credit creation:

Banks are the only financial entities that have the ability to generate credit or money. Banks not only produce money but also transfer it, unlike other financial entities. Deposits are created when banks make loans or advances. The idea of a deposit multiplier or money multiplier was born as a result. For instance: If a bank accepts a deposit of Rs. 1,000 and is required to maintain a CRR of 10%. The bank keeps 10% of this amount in cash reserves and may provide a loan of up to Rs. 900. The borrower of Rs. 900 may deposit the sum in either the same bank or a different bank, making the total amount deposited with the banks now Rs. 1,000+ Rs. 900. Until no bank in the financial system has reserves over the necessary 10% reserve, this procedure may continue. As a result, the economy will have a total money supply of Rs. 10,000. The term "money multiplier" or "deposit multiplier" refers to the proportion of fresh deposits to the initial rise in reserves[7], [8]. The multiplier is equal to the reciprocal of the reserve ratio, or 1/10, because it is 10/100. However, in practice, the banking system could not operate at its full potential because of leakages in the form of cash hoarding.responsibilities of commercial banks Among a commercial bank's duties are:

Deposit Acceptance

Commercial banks take deposits from people, businesses, and other organizations. Fixed deposit accounts, current accounts, and savings bank accounts are the three kinds of accounts where deposits are kept. A fixed account is one where funds are placed for a certain amount of time. Business organizations run current accounts where they may daily deposit and take money. Most people who run savings bank accounts do so because they are paid interest on their deposits[9], [10].

Loans that are advanced by banks are funded by deposits. Commercial banks often provide short-term loans for profitable endeavors. The function of banks has undergone significant change as a result of the nationalization of the commercial banks. To achieve economic goals, banks operating under RBI standards must adhere to the monetary policy. Banks provide a significant portion of loans to priority industries including exports, agriculture, and small-scale manufacturing.An increase in commercial banks Since 1806 till around 1969

The three Presidency banks the Bank of Bengal in Calcutta in 1806, the Bank of Bombay in 1840, and the Bank of Madras in 1843 were responsible for the birth of modern commercial banking in India. The second part of the 19th century saw the establishment of certain exchange banks. In 1935, the RBI was established. The RBI, the Imperial Bank, cooperative banks, exchange banks, and Indian joint stock banks made up the financial system in 1950. The banks were then divided up into scheduled banks. The Imperial Bank changed its name to the State Bank of India in 1955, and it was nationalized in 1959. In both urban and rural locations, the SBI operated branches. Fourteen significant commercial banks were nationalized in 1969. The lead bank program was established to provide financial services across the nation. Regional Rural Banks were founded in 1975 to meet the credit requirements of the less wealthy residents in rural regions. The expansion of commercial banking between 1951 and 1990 and 1996 and 2002 is explained by the following s.

Effect of Commercial Bank Nationalization:

The primary driver of India's banking sector expansion has been the nationalization of 14 major commercial banks. Fourteen significant commercial banks operating in the private

sector were nationalized in July 1969. It sought to provide financial services to rural locations and priority businesses including export, small-scale manufacturing, and agricultural. In terms of the national income, bank deposits increased from 15.5% in 1969 to 48.7% in 1999. Under the direction of F.K.F. Nariman, the RBI established a committee in August 1969, and it made the recommendation to launch Lead Bank in order to increase banking services in regions with little access to them. As part of this lead bank program, the SBI, 14 nationalized banks, and three private sector banks were each given a district. The Lead bank system has 580 districts nationwide at the end of 2002. Commercial banks' offices were in cities prior to nationalization. 60% of bank offices were constructed in rural regions after nationalization. Additionally, banks were formed in underdeveloped areas like as Orissa, Bihar, Madhya Pradesh, Assam, etc. Similar to this, bank deposits have significantly increased. From Rs. 3,399 crores in 1969 to Rs. 3,21,81 crore in 1998, the credit or advances also increased. 32% of the overall loan went to the priority sector.

Evaluation of Banking Following Nationalization:

Despite the commercial banks' remarkable success in terms of deposits, credit, offices, etc., the banking system nevertheless had several flaws and issues.

Principal issues with commercial banks:

Problem of Loan and Advance Recovery in Rural Areas:

One research claims that in 1993, past-due debts made about 50% of all bank loans. Insufficient bank locations and facilities: Even after nationalizing banks, our nation still struggles with inadequate financial infrastructure, especially in rural regions. Unsatisfactory bank performance: The profitability of the banks was severely damaged by the directed investment and directed loan programs, as well as increased spending. In 1990, several domestic and international banks suffered losses.

Advance Loans:

Banks provide loans using the funds deposited by depositors. The primary purpose of contemporary economies is this. Commercial banks have been providing short-term loans for productive uses. Banks now provide credit to customers. It is the financing provided by banks to buy consumer durables. Typically, banks provide their clients short- or medium-term loans.

Asset Classification

Banks have the following various asset classes:

i) Cash on hand and bank account balances
ii) Property held by the banking system
iii) Purchasing government bonds and other securities.
iv) Bank advances or credit.

Cash and government securities meet the banks' need for liquidity among the aforementioned assets. The most significant assets of the banks are the other ones, such as bank credit and investments in government securities.

The following are the three different kinds of investments made by commercial banks:

Investments in non-authorized securities and other securities that have been approved are also options.The first two kinds of securities are mandated by law for banks. More than 95% of all bank investments are in government securities, and the amount invested in other assets that have been authorized is negligible. However, because to the significant budget deficit, the

impact of the capital adequacy standards, and other factors, the investment in government securities is more than what is required by law. Therefore, the amount of government spending, bank resources, foreign capital inflows, demand for credit, etc., dictate these bank investments rather than necessarily the public vs. private sector ideology. Commercial paper, mutual funds, shares, and debentures of both public and private sector companies are all included in the third stage of investing. These are not legally required conditions for banks. In 2001-2002 and 2002-2003, respectively, the scheduled commercial banks invested Rs. 81000 crore and Rs. 92854 crores in these securities. Industry and commerce have relied heavily on bank loans or credit to fund their operations. As a result, banks lend money to small-scale companies, agriculture, and the education sector.

DISCUSSION

Classification of Liabilities of Banks

Demand deposits and term deposits are both accepted by Indian banks. Current deposits, saving deposits, and call deposits are additional categories for demand deposits. On demand payment is due for current deposits.

They are completely withdrawable by check. Most corporate enterprises have these deposits. On these deposits, banks don't charge interest. However, banks provide additional services to account holders, such as free out-of-town check collecting, demand draft issuance, dividend warrant issuance, and postal orders. Interest is paid on savings accounts. Checks may be drawn from a savings account, and the interest rate on these deposits typically varies from 4% to 6%. The number of withdrawals from this account, nevertheless, is limited. Demand deposits may include call deposits. They may be repaid on demand and are accepted from other banks. An interest is paid on these deposits.

These deposits, however, make up a relatively minor portion of all deposits.Term deposits and time deposits both exist. They are obligations for a certain period of time, which might range from a few days to a few years. They do not have the option of receiving checks, nor are they payable on demand. Only at the end of the maturity term for which these deposits are made may the funds put under this account be repaid. These deposits, however, are withdrawable before to maturity with a reduction in interest rate.

The liabilities side of a commercial bank's balance sheet is also made up of borrowings from other banks. Liabilities of banks include borrowings from the RBI, which is a significant component. mainly because it assesses the banks' resource sufficiency. 3% to 6% of overall liabilities come from borrowings from the RBI. In addition to these banks, other lenders include IDBI, NABARD, EXIM bank, etc.

Standards for Capital Adequacy and Non-Performing Assets

The issue of non-performing assets has been one of India's banking industry's most significant issues. Because it has an impact on the commercial banks' profits, it has drawn a lot of attention. The recent financial sector measures implemented to address it reflect the perception that this is the most difficult issue facing the banks. As banking grew throughout countries, rivalry among the banks of various nations started. The Capital Adequacy Norms are very important in the Indian context given the presence of nationalized banks. Commercial banks must adhere to these standards in order to preserve soundness and profitability in their operations. The Basel Committee recommended a number of standards for banks' risk management and minimum capital requirements. One of the issues facing the banking industry in the new century is risk management.

Unproductive Assets

The banking industry has long given much attention to the problem of NPAs. Numerous initiatives have been made to address the NPA issue. Describe NPA. Why do NPA issues develop? How big is it, exactly? What steps are being taken to address these issues? Let's go into more depth about this. The most challenging issue of non-performing assets in Indian banking is one that has attracted a lot of attention recently. The banking and financial industry has been grappling with what is seen to be its most difficult issue, and there have been significant attempts made to address it in recent years. The assets held by banks should provide positive returns in order to maintain the strengths and stability of banking systems. Assets that don't provide positive refunds are classified as non-performing assets. Non-performing assets, in a strict sense, are loans and advances that don't generate any revenue for the bank or add to its earnings. Non-performing assets, in a larger sense, include the workforce, physical assets, and unutilized cash reserves. Banks must keep some cash on hand, but this amount should be maintained to a minimum. The other assets, although equally significant, are not taken into account in this situation since we are only concerned with the profits on loans and advances. In India, NPAs were not well understood until recently. Overdue accounts were viewed differently by banks as NPAs. A unified definition wasn't adopted until the Narsimhan Committee Report was published. This committee would define non-performing assets as advances, whereby as of the balance sheet date:

a) With regard to term loans, interest is past due for more than 180 days;
b) When a bill is late and underpaid for more than 180 days in relation to invoices that were bought and reduced,
c) Cash credits and overdraft accounts stay inactive for a period of more than 180 days;

Non-performing assets are basically advances where interest and/or principal payments go unpaid for a period of two quarters or more. d) In regard to other accounts, any sum to be received stays past due for a period of more than 180 days. The R.B.I. established guidelines for NPAs. As a result, the banks are required to put aside a percentage of their assets as insurance against possible losses resulting from bad loans. Banks are required to reserve 10% of substandard assets. Provisioning for questionable assets is 20%, whereas provisioning for lost assets is 100%.

Size of the NPA

Growing NPA indicates that the locked money is either not being utilized effectively or not yielding sufficient returns. A bank may not make enough money to pay interest on deposits or repay principle if it has a high NPA rate.

According to a sector-by-sector examination of NPAs, private sector loans make up 44.49% of all NPAs at public sector banks, while non-priority sector loans make up 53.54%. The largest sector within the public sector bank group is SSIs, followed by agriculture (13.84%). It is evident that the non-priority sector is partly to blame for excessive NPAs.

Causes of NPA Growth

The following variables contribute to the buildup of NPAs: -

i) **Nationalization of Banks**: Following the nationalization of 14 major commercial banks in 1969, bank lending became commonplace and banks' business tenets were disregarded. This resolved the issue of debtors who were past due and in default.

ii) **Emergency of willful Default**: The phenomenon of wilful default has evolved as a result of the previous credit culture's decline. Even individuals who had no trouble paying back their loans began defaulting.

iii) **Industrial illness**: As a result of industrial illness, industrial sector debtors began making late payments. Business losses have been attributed to poor project planning, a lack of infrastructure, management issues, and marketing issues. Consequently, servicing bank debts suffered.

iv) **Inadequate Credit Monitoring**: Poor evaluation of the loan application, insufficient consideration of the project's commercial and financial viability, and insufficient credit monitoring were also to blame for the borrowers' poor performance and insufficient ability to repay the loans.

v) **Lack of Coordination:** When commercial banks and financial institutions worked together to fund huge projects, there was a lack of coordination that led to the NPA issue. Thus, a number of variables acting in concert have fueled the rise of non-performing assets at commercial banks.

Recommendations and Management of NPA Prevention

Recently, a number of initiatives have been started to minimize the number of commercial banks' NPAs. The list is as follows:

1. Accumulating Debt

Debt recovery courts: The Narsimhan Committee had advocated the establishment of special tribunals to shorten the time needed for setting cases involving defaulters. This might aid banks in swiftly pursuing claims against their customers and address issues. Debt recovery tribunals were formed when the suggestions were accepted.

2. Act on Securitization:

The Securitization and Reconstruction of Financial Asset and Enforcement of Security Interest law was enacted in an effort to lower NPAs. According to the Narsimhan Committee's suggestion, the law recommended the formation of Asset Reconstruction Companies.

This law included a clause allowing banks to get rid of poor debts. There was little advantage from this action, however. Asset Reconstruction Company of India Ltd., has eight stockholders, i.e.

With an initial capital of Rs. 10,000 crore, H.D.F.C. Bank, IDBI Bank, Federal Bank, South Indian Bank, S.B.I., IDBI, and ICICI Bank have been founded. A second feature of this law is the enforcement of security interests. Loan recovery remained a challenge even though debt recovery courts existed. As a result, this statute allows for the purchase of the security supplied for the loan within 60 days after providing notice on the defaulter and allows for the realization of value by putting the security away.

3. Bureau of Credit Information

A system of information is needed to stop loans from becoming non-performing assets (NPAs). All other banks must be made aware of a borrower's default with one bank in order for others to avoid lending to him. In this sense, a credit information bureau may be useful. It can keep a data bank that all landing institutions may access and evaluate. These actions have been taken by many developed and developing nations to address the issues with NPAs.

4. Adalat Lok:

A viable solution to the NPA issue is Lok Adalat, especially because it is effective in recovering minor loans. Lok Adalat may be scheduled by debt recovery tribunals for NPAs of Rs. 10 lac and higher.

5. Restructuring Corporate Debt

Reducing the debt load on the business sector via debt restructuring is another method for lowering NPAs. R.B.I. has established rules for this. Therefore, there would be three tiers in the corporate debt restructuring.

6. Settlements with Compromise:

A tool for the recovery of NPAs is also provided through the compromise settlement scheme. Guidelines were released by the R.B.I. in 1999, 2000, and 2001. The Rs. 10 crores in advances are subject to this measure. This applies to cases that have been filed with NPAs and those that are still ongoing with courts and DRTs. Fraud and willful default situations are excluded. Due to the underwhelming response to this program, the R.B.I. announced revised criteria and extended the deadline to April 30, 2003. The recovery of all scheduled commercial banks grew from Rs. 9716 crores in 1999 to Rs. 17588 crores in 2002 as a result of the steps taken to address the NPA issue. However, there hasn't been much progress in lowering NPAs.

Norms for Capital Adequacy

It is widely acknowledged that a key element in influencing the stability of the banking system is the bank's capital base. It is crucial to rebuild the capital foundation in India by following the rules since it has become so weak. According to data from the R.B.I., the ratio of bank deposits to paid-up capital and reserves had decreased from 6.7% in 1956 to 4.1% in 1961 and 2.1% in 1980. But in 1995, it rose to 7.53% as a consequence of capital adequacy standards. Basle Committee for Banking was designated as a supervisor by the Bank for International Settlement, Switzerland. Banks should have a certain amount of capital, according to the Basel Committee. In collaboration with representatives from fifteen developing economies, including India, the Basle Committee has developed several guiding principles. The capital adequacy ratio had been one of the committee's key concerns. A group headed by Narsimham was established by the R.B.I. to recommend resources for the financial industry. The Narsimham Committee's suggestions and those of the Basle Committee were identical. Prudential Norms are standards, laws, or regulations established by the nation's central bank. These regulations' primary goal is to safeguard depositors' interests. These standards differ from nation to nation. However, these guidelines are established in accordance with global norms. The main sources of revenue for banks are their lending and investing operations. Banks utilize deposit funds for these purposes. The interests of depositors are impacted if lending and investment choices are unsuccessful. Banks must utilize their resources effectively to address these issues while protecting depositors' interests. a capital adequacy ratio that is advised on a global and uniform basis. It measures the ratio between a bank's capital and its exposure to credit.To develop Capital Adequacy Norms, two forms of capital are needed as follows:

Financial capital that is more dependable and liquid makes up Tier I capital. It comprises of capital reserves, capital reserves, free reserves, and statutory reserves for banks. This is crucial capital for a bank since it protects the institution's interests and ensures the stability of the financial system.

Tier II Capital: This capital can sustain bank losses even if it provides less protection for depositors. It consists of capital investments, paid-up value of perpetual preference shares, asset revaluation, and subordinated debt. It is crucial to remember this. To reach the specified Capital Adequacy Norms, Tier II capital cannot be more than 50% of Tier I capital. The following are the Capital Adequacy Ratio standards established by the Basel Committee:

a) Tier I capital must represent no less than 4% of all risk-weighted credit exposures.
b) There must be a minimum of 8% of total capital to all risk-weighted capital exposures.

The banks must specify their Tier I and Tier II capital and provide the assets risk weights in accordance with the Basel Norms. The banks must then evaluate the capital to risk-weighted assets ratio. Indian banks are mandated to maintain a minimum CAR of 9%.

Risk-Based Asset

CAR measures the quantity of a bank's capital in proportion to the amount of risk-weighted assets, much as the ratios mentioned above. It considers the amount of risk associated with a bank's credit exposures; the higher the CAR, the more unexpected losses the bank can withstand before going bankrupt.

Managing Risk in Indian Banks

In order to help the banks make the transition to the CAN as painless and amicable as possible, the R.B.I. released a "Guidance Note on Management of Operational Risk" in October 2005.

The Basle Committee as Banking Supervisor announced "sound practices" for the management and supervision of operational risk in February 2003, and banks are urged to abide by them. NPAs are a concern for Indian banks as a result of their inability to effectively manage credit risk. Since banks must make provisions for NPAs in accordance with R.B.I. regulations, rising NPAs have a direct effect on bank profitability. In recent years, better banking practices among consumers have led to an increase in deposits. Under the shadow of banking sector reforms, however, banks are concerned about fully utilizing surplus liquidity out of concern about rising NPAs.The steps below assist banks in managing risk.

Management of Credit Risk

The management of a bank's credit risk is a crucial step. This NPA needs to be decreased. Credit risk management and non-performing assets are two distinct problems. Bank credit risk management is concerned with monitoring the quality of the credit portfolio before the defaults. NPAs are the outcome of a bank's previous lending strategy, where effect falls, or the bank's current condition, which produces risk. So, it represents an effort to prevent the default via responsible credit management.

Risk management includes:

For both market and credit concerns, the banks were urged to retain capital of at least 9% of their risk-weighted assets for both Held for Trading and Available for Sale.

In light of rising consumer and housing markets:

Steps were made to control credit and risk. In October 2004, the risk weights were raised from 50% to 75% for home loans and from 100% to 125% for consumer lending.

Decided

The complete amount of exposure the bank has to venture capital funds will be included in their capital market exposure as of April 2006, hence banks must now give these exposures a greater risk weight of 150%.

Reconstruction and securitization:

of the 2002 Act on Financial Assets and the Enforcement of Security Interests. The Indian government passed this Act in 2002 in order to lower NPAs and safeguard the interests of borrowers. A notice to settle the debt may be issued by banks to defaulters under this Act. The borrower has 60 days to pay off the debt. In addition, the lender may assume control of the borrower's assets.

Commercial banks are crucial to the financial and ultimately economic growth of a nation, whether it is developed or developing. Indian commercial banks must serve as both a profit-making institution and a growth-facilitating institution.

However, it struggles with NPAs. Indian banks must adhere to Capital Adequacy criteria in order to satisfy international standards. As a result, they have grown in size, become more technologically advanced, and have a stronger financial foundation. The Indian government has made several efforts to develop the country's banking industry. In 1991 and 1998, the Narsimham Committee suggested a number of changes for the banking industry. The prudential and capital adequacy standards must be adhered to by the banks.

The regulatory framework has made sure that India's banking industry is in excellent shape. The R.B.I. has made an effort to address the NPA issue with appropriate risk management measures. Commercial banks so continue to play a significant role in the Indian economy via CAN and risk management.

CONCLUSION

In conclusion, Due to its ability to facilitate the flow of funds from savers to borrowers, promote economic growth, and provide customers with essential financial services, commercial banking is essential to the financial ecosystem. Its ability to efficiently mobilize deposits, provide credit, and manage risks contributes to the stability and expansion of the economy as a whole. If commercial banks are to be relevant and valuable in the financial industry as technology continues to transform the banking environment and new problems occur, they must continue to be flexible, customer-focused, and forward-thinking. Policymakers and regulators must create an environment that supports ethical banking practices, innovation, and financial inclusion if commercial banking is to continue to be resilient and contribute to the greater economy. The dynamic economic environment, which includes interest rate fluctuations, business cycles, and geopolitical uncertainty, must also be navigated by commercial banks. Flexibility and excellent risk management are required to overcome these challenges.

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CHAPTER 9

A BRIEF STUDY ONNON-BANKING FINANCIAL COMPANIES

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ABSTRACT:

Non-Banking Financial Companies (NBFCs) have emerged as significant players in the financial sector, providing a wide range of financial services and bridging the gap between traditional banking institutions and unbanked segments of the population. This paper explores the role and significance of NBFCs in the financial system, examining their functions, regulatory framework, and the diverse products and services they offer. It delves into the unique challenges and opportunities faced by NBFCs, as well as their impact on financial inclusion, economic growth, and systemic stability. Understanding NBFCs is crucial for policymakers, investors, and consumers, as it facilitates informed decision-making, effective regulation, and the promotion of a robust and inclusive financial ecosystem.

KEYWORDS:

Asset Financing, Capital, Chit Funds, Consumer Finance, Deposit-taking NBFCs, Financial Services.

INTRODUCTION

Not Banking Financial intermediaries contribute significantly to the pace of expansion of the financial market. Consequently, a nation's pace of economic growth is boosted. NBFIs are crucial for boosting investment and saving. By mobilizing savings, closing credit gaps, and directing investments in the right areas, it has an impact on the economy. Indian financial intermediaries are often small, decentralized businesses with individual ownership. While others provide investors financial services, other NBFIs are involved in fund-based operations. Growth and varieties of NBFCs will be discussed after the review of NBFIs. Several different NBFC kinds, including mutual funds, UTI, & LIC, are discussed in length. Finally, this subject discusses the regulation of non-bank financial organizations, monetary policy, and NBFCs[1], [2].

Non-Bank Financial Institutions

Since the post-1995 era, there has been a significant change in how NBFCs operate. In India, there were several tiny NBFCs operating, but their information is unavailable. NBFCs carry out a variety of tasks in addition to providing investors with financial services. A financial intermediary is a company that gathers deposits and issues returns by investing the money in profitable ventures. They act as the intermediaries between lenders and borrowers. As a middleman, the NBFI also upholds security and liquidity throughout the resource mobilization process. By increasing the amount of saving and investing and by properly allocating money to profitable ventures, they play a significant role in the saving-investment process. Commercial banks often lack the resources necessary to meet a nation's and its investors' financial needs. The non-bank financial firms might expand as a result.An institution or company whose principal business is to accept deposits under any scheme or arrangement or in any other manner and lend in any manner," according to the RBI Act of 1997, is what is meant by an NBFC. In contrast to the preceding definition of NBFCs, this definition is thorough[3], [4].

Financial intermediary classification

Depending on the activities they engage in in their line of work, NBFCs come under a variety of categories.

1. Hire-purchase businesses
2. Investment Firms
3. Mutual Fund Organizations
4. Loan Businesses
5. Home Finance Organizations
6. Companies that finance equipment leasing
7. Remaining non-banking financing firms.
8. Various nonbanking businesses or chit fund firms

Let's get into more depth about what different types of NBFCs imply and how they work.

Companies that Finance Hire Purchase:

Hire buy financing may be obtained through a variety of sources, including:Retail and wholesale dealers, banks, and other financial institutions round out the list[5], [6].

Hire-purchase financing businesses are partnerships, public limited companies, or private limited corporations that provide credit for the acquisition of durable goods. A system known as hire purchase financing or credit allows for the advancement of term loans for the purchase of goods and services that must be repaid through an installment schedule. Depending on the goods, the hire buys credit's conditions may change. The down payment may be as much as 40% and is often between 10% and 25%. Typically, the credit period lasts for three years. Numerous goods and services are eligible for the hire purchase credit. Transport companies are the borrowers of a substantial portion of the hire buy financing made available for the acquisition of commercial vehicles[7], [8].

The second source of hire buy financing is retail and wholesale dealers. The sellers' sources of funding for hire-purchase credit are either their own money or loans from financial institutions. By offering installment loans, the financial institutions may fund either the buyers or the sellers. In addition to non-banking financial institutions, hire buy financing is also used by commercial banks, cooperative banks, and development financial organizations. These organizations include the Agro Industries Corporation, IDBI, ICICI, SFCs, and others[9], [10].

Investment firms

Large commercial or industrial groups dominate the control of investment corporations, and these organizations invest heavily in the firms that make up the industrial groupings to which they belong. These firms' primary activity is the acquisition and trading of securities. These businesses mostly provide financing to businesses connected to business houses. since these commercial organizations themselves constitute the firms. These businesses are close-end organizations with a set share capital, as opposed to open-end investment firms or mutual funds/unit trusts. The majority of significant industrial organizations have their own investment firms.

There are two types of investment companies:

Since 1996, Primary Dealers have been in operation. The number of PDs reached 15 at the end of March 2000. There are now 18 PDs. The purpose of PDS is to enhance the securities market, and the minimum Net Owned Fund is Rs. 50 crores. In order to enhance the risk

management system of PDs, the RBI issued new rules in January 2002. PDs are obliged to keep their CRAR at 15%. Considering the dangers of receiving deposits from other corporations. PDs are recommended to accept ICDs for no more than 50% of NOF. Dealers of satellites: SDs were first launched in December 1996 as second tier dealers. Nine SDs have registered accounts to trade government securities. Only 4 SDs are in use, therefore the response is constrained. Since May 31, 2002, the SD Scheme has been ended.

Mutual Fund Organizations

Loans are provided to people through Mutual Fund Companies or Nidhis without the need for a long application process. These businesses are accessible, and they tailor their loans to meet the demands of their clients. Share capita! deposits from their members, and public deposits are the sources of funding for Nidhis.

Loan providers

Loan firms are often small partnership businesses that take deposits from the public and use the money to provide loans to small businesses, independent contractors, and wholesale and retail dealers. These businesses entice the public to deposit money by providing higher interest rates together with other incentives, presents, etc. These businesses provide loans with comparatively higher interest rates. These businesses primarily take fixed deposits as deposits, keeping a portion of their cash in fixed deposits with banks and using the remainder to make loans and advances. Those who are unable to get appropriate credit from commercial banks are the ones that borrow money through these businesses.

homes Finance Companies: Mortgage loans are used to finance homes. It is one of the most crucial financial needs for middle class and middle-class people.

Housing finance businesses' roles are described.

1. Financing the purchase of a home.
2. Funding the building of a dwelling.
3. Paying for the purchase of a property parcel
4. Funding a home's renovation and expansion.

There are now more than 400 active home financing firms. The RBI has mandated that home financing businesses to mobilize consumer funds in the form of longer-term deposits.

DISCUSSION

Housing and Urban Development Corporation:

It is a national entity that provides loans to people and organizations for the construction of homes and apartments. 70% of HUDCO's loans are designated for rural regions, low-income groups, and economically disadvantaged individuals. Up till March 1993, HUDCO has provided funding for 9,420 projects totaling Rs. 12,490 crores. This required the building of 5. Out of the 5 million homes, 46% are found in rural regions.

Limited by the Housing Development Finance Corporation

This home financing organization operates on a nationwide scale. It was established in 1977 to provide term financing to middle class and lower income groups for the building of homes, the purchase of homes, etc. HDFC approved home loans of Rs. 4,470 crores up till March 1993.Those who finance state-owned housing:

These organizations have been set up in every State, and they provide connected main co-operative housing societies with loans for the building of homes, the acquisition of land, and the repayment of mortgage debt.

Subsidiaries of Housing Finance:

such as Can Fin. Other companies that offered home loans were 11011705 Limited, GIC Grih Vitt Limited, State Bank home Finance Corporation, and LIC Housing Finance Limited Company.

Companies that finance equipment leasing:

It involves a contract that divides and divides the risk-taking, ownership, and financing of any equipment or asset between two or more parties. In a leasing firm, the user of capital equipment merely purchases the use of the item in exchange for paying a leasing company that owns the item a monthly rental price. Due to rising investment demands and a lack of funding in public financial institutions, India's leasing industry has significant prospects.

Non-banking Residuary Finance Companies:

These are businesses that accept deposits but do not fall under any of the other NBFC categories. There are many unfavorable aspects of these businesses, includingas :

1. NOF that is negative or negligible.
2. They overstated the amount of deposits they owed.
3. Deposit forfeiture.
4. Deposit certificates are no longer being issued.
5. Low rates of deposit return.
6. Payment of high commission rates
7. Service fee assessed to deposits.

The apex has implemented a variety of measures to get rid of these characteristics. For example, under the new regulatory framework established by the RBI Act of 1997, the RBI has extended prudential norm-3 to these companies, imposed a requirement for mandatory registration, and specified the minimum rates of interest that must be paid on deposits made under various schemes. The RBI has increased the examination and oversight of these firms' operations.

Causes of NBFC Growth

1. NBFCs provide investors services that are ready to use.
2. Compared to banks, NBFCs are subject to relatively less regulation.
3. more customer-centeredness in approach.
4. Speed and simplicity of their offerings.
5. High interest rates for modest savers' deposits.

Issues with NBFCs

The NBFC may not follow the RBI's instructions. As a result, the goals of monetary policy could not be achieved. Offering of High Rate of Interest: NBFCs may initially give investors a high rate of interest but later on, owing to a difficulty, they may not be able to continue doing so. There are several leaks in NBFCs since every turnover period, the full money is routed via the banking system, and only the amount of savings that is assigned to the NBFI is routed through the income turnover period. In other words, banks supply the people's surplus

cash, while NBFIs serve as a conduit for converting savings into investments. All of these factors put banks and non-bank financial firms in rivalry with one another.

Financial Policy and NBFCs

Before 1997, there was no regulation of NBFCs. The 1997 amendment to the RBI Act created a regulatory framework for NBFC operation. In the past, NBFCs offered their investors huge interest rates. They were seen as posing a danger to the RBI's monetary policy's ability to operate. Second, NBFCs were providing loans to those who had been denied credit by banks. The NBFC's efficacy was impacted as a consequence. Therefore, recommendations were made that NBFCs, like commercial and cooperative banks, should be subject to monetary restrictions. Thus, the RBI has the same authority to provide directions and recommendations to NBFCs as it does to banks. The RBI uses a variety of credit control techniques to exert its authority to restrict NBFC activity. Since 1997, oversees the operation of NBFCs for their healthy development using tools including prudential rules, interest rate ceilings, registration of NBFCs, etc.

NBFIs' Effect on India's

Financial intermediaries are crucial to the growth of a nation's economy. The money market has to be expanded if economic development is to be at its greatest pace. There is still room for the money market to flourish in India. These are the primary duties of financial intermediaries:

Growth in Investment and Saving

People's deposits are collected by financial intermediaries, who then lend the institutions money to fund loans to borrowers. Savings are thus directed toward the process of investing. High savings and investment rates are required for rapid economic growth.

Aids Beginning Investors:

Direct securities are purchased by an intermediary in the denominations that the eventual borrowers choose. Small investors may often avoid purchasing securities directly from issuers. In this way, financial intermediaries might act as a bridge between investors and borrowers.

Flexibility in the Assets' Maturity:

People often choose to invest in short-term financial assets, but borrowers need funding for long-term needs. Financial intermediaries are in charge of filling up the gaps between the two parties' preferred time frames.

Enhanced Liquidity

Financial intermediaries provide the option to withdraw money prior to the financial asset's maturity time. The assets are more liquid as a result.

Low danger and security:

Financial intermediaries reduce the investment risks. Similar to this, money invested with financial intermediaries is quite secure and offers a respectable rate of return.Financial intermediaries have several locations spread out across a large region. Banks, LIC, and UTI have handy locations in various areas.The numerous investment strategies are described by financial intermediaries. Additionally, they analyze securities and their benefits for investors.Village money lenders engage in unethical behavior including charging exorbitant

interest rates on loans and other forms of deception. The financial intermediaries refrain from engaging in these tactics. The NBFCs' significance to economic growth was discussed above. NBFIs have played a significant part in helping India achieve a high rate of saving and investment. High investment rates have been attained in India owing to the rise of the NBFC-dominated money market, which is one of the two wheels that propel economic growth in a nation.

Control of NBFCs

The NBFCs have contributed significantly to the financial and economic growth of a nation. There have, however, been certain flaws in them.

Issues with NBFC

1. NBFC may not operate in accordance with RBI instructions. This may prevent the RBI's monetary policy from achieving its goals.
2. Offering a High Interest Rate.
3. NBFC may initially provide investors with high rates of interest, but later on they may not be able to.
4. Breach in NBFCs.

This occurs because every turnover period, the full money passes through the banking system; only the amount designated to NBFCs travels through the income turnover period. In other words, banks give the people's surplus cash, while NBFCs serve as a conduit for converting their savings into investments. All of this encourages rivalry between banks and financial entities that are not banks. Therefore, the RBI controls its operations in accordance with the following: The Reserve Bank of India Act, 1997, which was passed, gave the RBI authority over NBFCs.

RBI'S Instructions and Rules for NBFC Regulation

Investment Funds:

A mutual fund is a middleman that purchases or sells securities on behalf of the people who own its units. Considering that unit owners would not be able to acquire or sell shares in an affordable and profitable manner. It is a crucial NBFI type that mobilizes savings. In India, the first MF was founded in 1964.

The Unit Trust of India was its name. Small- and middle-income workers may benefit from MF by receiving a high rate of return on their money. MFs may be roughly categorized as belonging to the public or private sectors. Public sector MFs include all those supported by banks, the UTI, and other financial organizations. Other MFs, which date back to 1993, are known as private MFs. The UTI is significant to MF's operations in India. When it was founded in 1964, IDBI controlled 50% of its share capital, while the remaining 35% was contributed by the LIC, SBI, scheduled commercial banks, IFCI, and ICICI.

Indian Unit Trust

Early in the 20th century, unit trusts were recognized for their use in mobilizing small investors' money, and the Shroff Committee emphasized their relevance in 1954. But the Unit Trust of India didn't start operating as a public sector financial entity until 1964.

Initial Investment:

Unit Trust's starting capital was legally required to be Rs. 5 crores, which was to be supplied by the Reserve Bank, the LIC, the SBI, the Associate Banks, and other banks and financial

organizations. Due to the Trust's lack of share capital, it operates on the "no profit, no loss" tenet, with all profits and income going to investors after all expenses and development fees have been paid.

Unit Capital

The cash collected via the sale of units to the general public under different schemes serves as the UTI's primary funding source. For instance, under the Unit Scheme of 1964, units are sold at a face value of Rs. 10 apiece, even if their market price is greater.

UTI-Related Issues

Following the collapse of UTI's US-64 Scheme, the government made efforts to address the issue and safeguard the investors in 2001–2002. Numerous structural changes were made by the government. A few of them are expressed.In June 1999, the government repurchased shares of PSEs from UTI under the Special Unit Scheme at a price above the going market rate. This significantly aided in the flow of funds to investors in the US-64.Investors were granted a limited repurchase option, allowing them to sell up to 3000 units back to UTI at a price set by the administrative staff. The government would pay the UTI the difference for each unit it repurchased from the UTI at a price higher than its net asset value.

Extended Repurchase Facility

The 3000-unit cap was increased to 5000 units in December 2001. Additionally, investors who purchased more than 5000 units were guaranteed to get the greater of the NAV or Rs. 10 if they were still alive in May 2003. The difference between the buyback price and the UTI's NAV would be covered by the government.

Insurance Organizations:

An insurance corporation has both financial and humanitarian goals. The administrative and marketing expenses are covered by the premium that insurance firms charge. They provide their investors with protection in exchange. The insurance industry involves dispersing risk over time, across individuals and organizations. Mortality legislation governs life insurance.

The following are the regions where insurance companies operate:

1. Health
2. Life
3. General.

Since 1818, life insurance has been a thing in India. In Calcutta, Oriental Insurance firm, the first insurance firm was founded. The General Insurance Company has been around since 1850. The size and organizational structure of insurance firms are described here.

Investment Behavior

The LIC Act of 1956 mandates that the corporation invest 50% of its funds in bonds and debentures issued by the Central and State governments, 25% in semi-government and the public sector, and 10% in the cooperative sector. For the benefit of the policyholders, it makes direct investments in corporate shares and debentures.

Insurance Businesses

There are now 24 insurance companies, including two state-owned firms. In 2001–02, LIC and GIC together paid insurance premiums of Rs. 62,477 crores. TheFrom 7.6% in 1980 to

10.1% in 1990 and 12% in 2001, the insurance sector's proportion of household savings has increased. In all of these years, the insurance sector's contribution has been 0.6%. The uptake of insurance, however, has remained low at 2%.

Corporation for Life Insurance:

After the nationalization and merging of 250 separate life insurance businesses, LIC was founded in 1956. Its main office is in Mumbai. Its main goal is to provide individuals access to life insurance coverage. It encourages saving as well. Additionally, it offers investors income tax breaks.Thus, LIC mobilizes the people's money and ensures their financial futures by offering them substantial returns on their investments via its many programs, policies, and plans. People may also withdraw funds that they have invested in various plans or policies. Additionally, there is the security of LIC investment. Senior folks are similarly covered by various programs and pension plans. About 18% of its policies are for protection, while 60% are for savings. There are 37 new insurance options from LIC. It has 2,048 branch offices, 1,774 branches, seven zonal offices, 100 divisional offices, and around 6.28 lakh agents. As of right now, the entire investment in individual life insurance in 2000–01 was Rs. 1,75,491 crore, while the total premium revenue from group insurance was Rs. 3,133 crore. Through the mobilization of rural savings, LIC has also had a significant impact on rural areas.

Corporate General Insurance:

The government controls GIC, which has four companies, including

1. Countrywide Insurance Co. Ltd.,
2. Insurer New India Co. Ltd.,
3. Insurance company called Oriental Fire and General. Ltd.

Company named United India Insurance. Ltd. 'Fire insurance' is the primary line of business for GIC, followed by ‘marine business' and 'other business. GIC operates in accordance with the 1938 Insurance Act's provisions. The premium earnings, reserves, paid-up capital, and profits make up GIC's funding sources. The GIC policies are different from the LIC's financial claims. GIC policies are valid for at least a year. GIC focuses on industries including fire, car, marine, aviation, theft, loss, and damage, among others. In 1985, it had established cooperative insurance. GIC satisfies the demands of the residential, agricultural, and industrial sectors.

The primary business activity of NBFCs is accepting deposits under various programs and disbursing loans in various forms. NBFCs come in eight distinct varieties. The commercial banks provide them with fierce competition. One of the most important NBFCs are the lending companies. Similar to this, key categories of NBFCs such equipment leasing companies and housing finance companies have formed. NBFCs are subject to extensive regulation under the RBI Act of 1997. This Act states that NBFCs must get a registration certificate from the RBI in order to do business. They must also follow all guidelines on public deposits, prudential standards, and liquid assets. Additionally, the RBI obliged them to make quarterly returns.

CONCLUSION

In conclusion, Non-Banking Financial Companies have established themselves as crucial actors in the Indian financial industry, enhancing conventional banking institutions and fostering financial inclusion.

Their adaptability, creativity, and customer-focused mindset all help the financial ecosystem be more resilient and productive overall. To guarantee the continuing expansion and stability of NBFCs, policymakers and regulators must find a balance between encouraging innovation and addressing systemic risks. Consumers and investors should base their judgments on the reputation of the NBFCs they work with as well as prudential standards. NBFCs may continue to make substantial contributions to economic development, financial inclusion, and the general well-being of society by tackling problems and seizing opportunities. Although NBFCs provide chances for financial inclusion, they must also respect strict guidelines for governance, openness, and responsible lending. The sustained development of NBFCs depends on treating consumers fairly and ethically.

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CHAPTER 10

EXPLORES THE RELATIONSHIP BETWEEN FINANCIAL MARKETS AND MONEY MARKET

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ABSTRACT:

The financial market plays a crucial role in facilitating the allocation of funds and enabling economic growth. Among its key components, the money market serves as a vital platform for short-term borrowing and lending, contributing to overall monetary stability and liquidity management. This abstract delves into the concept of the money market, its significance in the financial ecosystem, and its impact on various economic agents. Through an analysis of its key characteristics, instruments, and functions, this abstract shed light on the role of the money market in maintaining financial equilibrium and providing essential funding opportunities for both governments and corporations. Furthermore, it explores the relationship between the money market and central bank policies, highlighting the measures taken by authorities to regulate and stabilize these markets during periods of financial turbulence. Overall, this abstract emphasizes the essential role of the money market in sustaining the financial system's smooth operation, fostering economic development, and maintaining monetary stability.

KEYWORDS:

Bonds, Capital Markets, Commodities, Derivatives, Equity Market.

INTRODUCTION

The money market is a section of the financial markets for assets used for one-year or shorter initial maturities of short-term borrowing and lending. Treasury bills, commercial papers, certificates of deposit, federal funds, and short-term mortgage and asset-backed securities are all traded in the money markets. It finances the global financial system with liquid assets.Financial institutions and credit dealers that want to either lend or borrow make up the money market. Participants lend and borrow money for brief durations, usually up to thirteen months. Short-term financial products are traded in the money market and are referred to aspaper. In contrast, bonds and stock are provided by the financial market for longer-term financing. Banks' lending to and borrowing from one another via repurchase agreements, commercial paper, and other similar products makes up the majority of the money market[1], [2].

The lending and borrowing of short-term cash are part of the India money market's monetary system. Just after the globalization drive in 1992, the Indian money market saw exponential expansion. Financial institutions have been shown to use money market instruments to meet the short-term cash needs of numerous industries, including manufacturing, banking, and agriculture. Over the last 20 years, the money market in India has performed magnificently. The Reserve Bank of India, the nation's central bank, has traditionally played a significant part in governing and managing the Indian money market[3], [4]. The RBI may intervene in a variety of ways, including as decreasing the cash reserve ratio to stave off crises or injecting more money into the economy. A market for lending and borrowing short-term cash is known as the money market. It deals in investments and financial products with a one-year or shorter maturity term. It encompasses cash and near substitutes for cash in the form of financial

assets. It is a telephone-based activity rather than a location. It is a collection of markets covering seven products, including the call money market, commercial bill market, and others, rather than a single market. It is a wholesale market for instruments of short-term debt[5], [6]. The Reserve Bank of India, mutual funds, bar corporate investors, non-banking finance firms, state governments, provident funds, primary dealers, Securities Trading Corporation of India, and public sector undertakings are the major participants in the money market. The Indian money market's most significant element is the Reserve Bank of India. The direct jurisdiction of RBI regulation extends to the money market. The goal of RBI money market operations is to maintain liquidity and short-term interest rates at the levels necessary for attaining monetary policy goals. The main goals of monetary policy are to promote price stability and economic development[7], [8].

Uses of the Money Market

One of the money market's key roles is to offer a mechanism for achieving equilibrium between the supply and demand for short-term funds.

1. It also gives the government money to cover deficits in a non-inflationary manner.
2. It offers several opportunities for short-term capital investments with reasonable returns.
3. It assists the RBI in carrying out monetary policy effectively.

Indian Money Market Structure

Both the organized sector and the unorganized sector make up the Indian money market. The RBI is the key player in the Indian money market. The RBI has direct authority to regulate the organized sector. Local bankers, money lenders, and unregulated non-banking financial organizations make up the unorganized sector.A single market does not exist in the organized money market. It comprises of a variety of markets, including markets for CDs, CPs, and repos, as well as the call money market, treasury bill market, commercial bill market, and others. Numerous products are traded in the money market, including call money, treasury bills, commercial bills, CDs, CPs, and repos. With the establishment of Money Market Mutual Funds and The Discount and Finance House of India, the Organised money market has become even more varied[9], [10].

1. The Call Money Market:

Mumbai, Calcutta, and Madras are the key hubs for the Call Money Market. Fluids are borrowed and lent on the call money market just for that specific day. Within 24 hours, the cash may be called back. The Inter Bank Loan Market is another name for the Call Money Market. This market is served by Scheduled Commercial Banks, Co-operative Banks, and the Finance House of India. As lenders, organizations like LIC, GIC, UTI, IDBI, & NABARD are permitted to run the call money market. The State Bank of India is almost always on the market's lender side. The call money market is very sensitive and serves as the best gauge of the money market's liquidity condition.

2. The Treasury Bill Market:

Treasury Bills are traded on this market. Treasury Bills are the Central Government of India's short-term obligations, with terms ranging between 91,182 and 364 days. In India, the treasury bill market is still in its infancy. The RIM just holds these banknotes in a passive capacity. 90% of the outstanding Treasury Bills are held by the Reserve Bank. The RBI is required by law to take any Treasury bills that the government offers to sell to it. The treasury

bills that banks and other entities submit to it must also be rediscounted. This led to the monetization of the national debt, which increased the money supply inflationary.

3. Repo Market:

The repo market is a kind of money market that facilitates the selling and purchase of debt instruments to facilitate collateralized short-term borrowing and lending. Now, the repo market has expanded. Now, in addition to Central Government bills and securities, it also includes State Government securities, Public Sector Undertakings, and Private Corporate Sector assets. Repos have been used to stop speculative behavior during periods of foreign currency volatility when money flows from the money market to the foreign exchange market.

4. The Commercial Bill Market:

Commercial bills are exchanged inside this particular submarket. The bills written by the seller to the buyer are the commercial bills. A commercial bill's objective is to pay the seller back while the customer postpones payment. Through its Bill Market Schemes between 1952 and 1970, the RBI has made attempts to establish the bill market in India and promote the usage of bills. However, the commercial market in India is sadly undeveloped. The prevalent cash credit system of bank lending is the main impediment to the growth of bill financing in our nation. The RBI urged banks in October 1997 that at least 25% of borrowers' inland credit purchases should be made via bills in order to promote the "bills" culture.

5. The Certificate of Deposit Market:

The RBI launched Certificates of Deposit in 1989 to increase investor flexibility and broaden the selection of products available in the money market. Only commercial banks are permitted to offer CDs in multiples of Rs. 25 lakhs. An issuance should have a minimum size of Rs. 1 crore. The maturity of CDs may range from three months to a year. By endorsement, the CDs may be freely transferred. On CDs, the banks provide hefty interest rates. In 1992, CDs having maturities of more than a year and up to three years were allowed to be issued by IDBI, ICICI, IFCI, and IRBI. Two other organizationsthe Export-Import Bank of India and the Small Industries Development Bank of Indiawere given permission to issue CDs in 1993. The face value of CDs is discounted when they are issued, and the discount rate is freely chosen. CDs may be sent and transferred without restriction. The money market's ample liquidity circumstances caused the interest rates on CDs to decrease in 1996–1997.

In 1990, the commercial paper market was established. A listed business with a working capital of at least Rs. 5 crores may issue the commercial paper. They could be distributed in increments of Rs. 25 lakhs. The smallest size of an issue is one crore rupees. Every six months, the firm seeking to issue CP must receive a certain rating from an organization that has been authorized by the RBI. CPs may be delivered and transferred without restriction. CP takes between three and six months to reach full maturity. The actual interest rate has often ranged from 9.35% to 20.9% p.a.Money Market Mutual Funds: In April 1992, the RBI established MMMFS. The major goal was to provide ordinary investors another short-term option. In 1995, the RBI approved a few leniencies to improve the scheme's allure. Their size and investment restrictions have been loosened. MMMFS may be set up by banks, governmental financial institutions, and private sector organizations. Since 1996, MMMFS have had the same rights as other mutual funds to offer units to corporations and other organizations. Since March 7, 2000, MMMFS have been subject to a preview of SEBI rules. Although the organized portion of the Indian money market is somewhat integrated and organized, it cannot be compared to the money markets in London and New York.

DISCUSSION

The Unorganized Sector

1. Indigenous Bankers

Indigenous bankers are people or private businesses who act as banks by accepting deposits, disbursing loans, and so on. They are considered to be part of the unorganized sector of the money market since their actions are not regulated. Native bankers vary from money lenders in that they accept deposits and deal in dollars in addition to providing loans, while money lenders solely make loans and do not accept deposits or deal in dollars. Native American banks are not a uniform bunch. They fall broadly into one of four categories: Gujarat shroffs, Multani or Shikarpuri shroffs, Marwari Kayas, or Chettiars. The local banks do not want to distinguish between banking and non-banking activity. Their inclusion into the organized financial system has been hindered by this. The extremely high interest rates charged by the domestic banks are unaffected by the RBI's bank rate policy. The geographic scope of native bankers' activities has shrunk over the last 20 years as a result of the expansion of commercial and cooperative banking.

Strengths, Weaknesses, and Characteristics of the Indian Money Market

1. The existence of an unorganized money market:

Makes it difficult for the RBI to exert control over the money market due to the dichotomy between the organized and unorganized sectors of the Indian money market. There is no distinction between short-term and long-term financing in the unorganized market. The RBI's requirements have not been adopted by the local lenders. The RBI has minimal control over the money market since these bankers and NBFCs operate outside of the organized money market.

2. Lack of Integration:

Both the numerous submarkets and the many entities and agencies that make up the money market lack proper integration. Between cooperative banks, commercial banks, state banks, and foreign banks, there is less coordination. Banks that are cooperative and commercial compete with one another. The local banks operate in a certain manner.

3. Multiplicity of Interest Rates:

Another flaw in the Indian money market is the occurrence of too many interest rates. Even for the same sort of loan, interest rates in the unorganized money market vary significantly from region to region. Government borrowing rates, deposit and lending rates at commercial and cooperative banks, etc., all vary. The lack of integration between the different elements of the money market is the cause of the variety in interest rates. A major factor in the diversity of interest rates is the immobility of funds from one money market to another. The interest rate structure must be efficiently rationalized and managed by the RBI.

4. Lack of Organized Bill Market:

Although domestic and international bills are bought and sold by commercial banks, there is no organized bill market in the nation. Under its 1952 and 1970 programs, the RBI only succeeded in creating a small amount of the bill market. These plans fell short of creating a bill market across the nation. There is a serious lack of business bills. The prevalence of cash credit and the inconsistency of commercial bills proved to be significant roadblocks to the

growth of the bill industry. From 20.3% in 1971 to 9.1% in 1997–98, the bill financing has decreased.

5. Lack of cash:

Lack of funds is a defining feature of the Indian money market. The supply of loanable cash cannot keep up with the demand.

The lack of financial resources is also brought on by little savings brought on by low per capita income, a lack of banking habits, poor banking infrastructure, and the formation of a parallel economy.

6. Seasonal Financial Constraints

Another disadvantage of the money market is the seasonality of the funding supply. Wide seasonal swings in interest rates have been brought about by this. More money is needed during the busiest season. Interest rates are high and there is a monetary squeeze on the market.

But interest rates significantly decrease during the slow season. The call money market remained very volatile notwithstanding the efforts made by the RBI to reduce rate swings.

7. Inadequate Banking Infrastructure

Despite the widespread opening of commercial banks, our nation's financial infrastructure is still insufficient. The countryside is not included. In India, there is one commercial bank branch for per 15,000 people, compared to one for every 1200 people in the US. Poverty causes people to have modest funds, which are harder to access

The Indian money market lacks a variety of sub-markets and is underdeveloped. It does not draw in outside capital. It cannot be compared to the sophisticated money markets in London and New York.

Restructuring Steps to Grow the Indian Money Market

The RBI launched many policy initiatives to expand the money market. At least in the organized sector, the Indian money market is now intertwined. The RBI has started a number of changes based on the recommendations of the Sukhmoy Chakravorty Committee and the Narsimhan Committee.

1. Laxer controls on interest rates:

Banks have been urged to make sure that any changes to interest rates stay within acceptable bounds. Interest rates have been further liberalized as a result of the Narasimhan Committee's recommendations from November 1991, and banks and financial institutions have been instructed to choose and implement market-related interest rates.

The RBI kept lowering the bank rate from 10% in 1990–1991 to 6% in 2003–2004 in an effort to boost the economy and liquidity.

2. Call and Term Money Market Reforms:

To increase liquidity, the RBJ liberalized call money market entrance throughout the 1990s. As of right now, only a few non-banking financial institutions and mutual funds are acting as borrowers; banks and primary dealers, on the other hand, are acting as both lenders and borrowers. The RBI has also eliminated the restrictions in the term money market.

3. The addition of new instruments to the money market

a. In the money market, 182 day Treasury bills, 364 day Treasury bills, and certificates of deposits are the four main new securities. The number of CDs issued by commercial banks has increased significantly. Since 1992, there has been a tremendous advancement in the CPs main market. To establish dated securities as a financial tool, the government has chosen to offer them at auction.The high stamp duty on usance bills was seen to be a significant deterrent in the bill market. The government removed the stamp duty from the purchase bill in August 1989.The RBI deregulated money market interest rates as of May 1, 1989. This is a significant step in the money market's activation.

4. Refinancing from the RBI:

To address liquidity issues and regulate credit conditions, the RBI provided refinancing facilities to a number of industries. There are now two refinancing options available: general refinancing and export credit financing. The refinancing rate remains tethered to the bank rate according to the RBI.

5. Money Market Mutual Funds:

The government announced the creation of money market mutual funds in April 1992 with the goal of making money market instruments accessible to everyone. Three MMMFs have so far been established, one each by the IDBI, UTI, and the private sector.

6. The Discount & Finance House of India:

On April 25, 1988, The Discount & Finance House of India was founded. Its primary purpose is to integrate all of India's financial institutions, including those in the public and private sectors, scheduled commercial banks, foreign banks, cooperative banks, and other financial institutions, into the Indian Money Market. The DFHI has actively participated in the short-term money market and significantly aided in maintaining market stability overall.

7. Repos's debut:

Repos was first made available in December 1992. It is a buyback agreement mechanism used by the RBI and commercial banks. Due to its ability to manage short-term liquidity, it has recently gained popularity among banks and financial organizations. The market determines the repo rates, and since 1993, the repo period has stabilized at 14 days. In April 1999, the RBI enacted new regulatory measures to expand Repos. Since November 1996, the Reserve Repos program has allowed investors to buy dated government assets at a preset cut-off interest rate via an auction. This reserve and repos use policy Liquidity Adjustment Facility is the name for repos. Since 2000–2001, LAF has become a significant monetary policy tool.

The money market is a section of the financial markets for assets used for one-year or shorter initial maturities of short-term borrowing and lending. Federal funds, short-term mortgage and asset-backed securities, commercial papers, certificates of deposit, Treasury bills, and commercial and Treasury bills are all included. It finances the global financial system with liquid assets. The direct jurisdiction of RBI regulation extends to the money market. The goal of RBI money market operations is to maintain liquidity and short-term interest rates at the levels necessary for attaining monetary policy goals. Both the organized sector and the unorganized sector make up the Indian money market. Call money market, treasury bill market, commercial bill market, markets for CDs, CPs, and repos are just a few of the

markets that make up the organized money market. The establishment of The Discount and Finance House of India and Money Market Mutual Funds further diversifies it.

CONCLUSION

In conclusion, the money market plays a crucial role in the global financial system by giving different economic players access to liquidity and short-term financing options. Its effective operation requires a complex balancing act between market forces and regulatory actions in order to maintain economic stability. Policymakers and financial institutions may cooperate to promote a resilient and strong financial environment supportive of economic success by comprehending and managing the complexity of the money market. The money market does not come without hazards, despite its enormous benefits. To prevent possible crises, financial institutions must constantly monitor counterparty risk and market volatility. Furthermore, regulatory agencies should keep an eye on changes in the money market in order to address any developing systemic issues and advance market transparency.

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CHAPTER 11

ANALYZES THE CHALLENGES AND OPPORTUNITIES FACING THE CAPITAL MARKET

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ABSTRACT:

The capital market serves as a vital component of the financial system, facilitating the issuance and trading of long-term financial instruments, such as stocks, bonds, and derivatives. This paper explores the key aspects of the capital market, including its functions, role in financing economic growth, and the diverse investment opportunities it offers to investors. It delves into the significance of primary and secondary markets, as well as the regulatory framework that governs capital market activities. The study also analyzes the challenges and opportunities facing the capital market in a dynamic and interconnected global economy. Understanding the capital market is essential for policymakers, investors, and businesses, as it enables informed decision-making, effective risk management, and the promotion of sustainable and efficient capital allocation.

KEYWORDS:

Commodity Derivatives, Credit Rating, Demat Account, Direct Tax, Foreign Direct.

INTRODUCTION

The capital market is where long-term investments are made. It alludes to the institutional setups and facilities for borrowing and lending term money. Government, business, agriculture, and the industrial sector are the key sources of long-term funding needs. The federal and state governments invest in both basic and consumer goods sectors in addition to economic overheads like transportation, irrigation, and power supply, necessitating a significant amount of capital market funding. The majority of the money supply originates from private and corporate savings, government, banks, insurance firms, and other specialized financial organizations[1], [2].

Function And Importance of Capital Market the Economic Development of India

The capital market is very important for capital creation. A quick economic growth is dependent on enough capital generation. The capital market's primary purpose is to gather funds and distribute them for industrial growth. This encourages capital creation and quickens the pace of economic growth[3], [4].

1. **Mobilization of savings and acceleration of capital formation**: The capital market's diverse securities enable to mobilize savings from a range of demographic segments. Two key characteristics that encourage investors to purchase securities are a reasonable rate of return and liquidity. This quickens capital creation, which supports economic growth[5], [6].

2. **Long-term capital:** Companies may raise long-term capital via the stock exchange market. Investors cannot commit their money for a lengthy period of time, while businesses need permanent cash. Investors have the chance to acquire and sell securities on the capital market without affecting the permanent capital[7], [8].

3. **Industrial development:** The stock market encourages individuals to invest in profitable ventures as opposed to unprofitable ones like gold, real estate, etc. The stock market sends money to the industrial sector, promoting economic growth and industrial expansion.

4. **Appropriate channeling of funds**: An effective capital market generates liquidity and distributes resources to the most productive sectors of the economy. People choose a firm to invest their money in based on the security's yield and market price. This makes it possible to use money effectively[9], [10].

5. **Ready and Continuous Market:** Due to the ease of marketability, investments in securities are more liquid. Securities may be bought and sold by buyers and sellers with ease.

6. **Offering a range of services**: Financial institutions in the capital market provide a range of services, including:

i. Lending to company owners for medium- and long-term loans to start, grow, or upgrade their operations.
ii. Participation in equity financing,
iii. Facilities for underwriting.
iv. Support for business marketing.
v. Professional guidance on handling investments in industrial securities.

The amount of capital market transactions has dramatically expanded during the last 20 years. The activities of the capital market have changed. Investments have multiplied phenomenally, keeping up with the rapid pace of economic growth.

Composition and Structure of the Capital Market

Similar to how the money market is the market for short-term funds, the capital market is the market for long-term funds. All institutional setups and facilities for long-term borrowing and lending are included. Private commercial firms, public businesses, and the government all need long-term money capital. Individual and institutional investors, banks, and specialized industrial finance organizations provide the capital market with money.

Overview of Indian Capital Market History

The East India Company stocks were first traded in India in the eighteenth century, beginning the country's capital market's history. Securities trade remained unorganized till the end of the nineteenth century, and Bombay and Calcutta were the primary trading hubs. Bombay was the main trading hub for the two, with bank shares being the main trading stock there. Bombay played a significant role in the supply of cotton during the American Civil War. As a consequence, trading activity were abundant over the time period, which caused a surge in share prices. This boom, the first in the Indian stock market's history, lasted for over five years. On July 1, 1865, there was a dramatic drop in share values, which caused the bubble to collapse. Twelve brokers were the only ones allowed to trade at the time, and they did so in front of Bombay's Town Hall beneath a banyan tree. In 1875, these stock dealers established the Native Shares and Stock dealers Association, Bombay, as an unofficial organization. Later, in industrial and commerce hubs like Calcutta and Ahmedabad, stock markets emerged. The Bombay Securities Contracts Control Act, 1925 authorized the establishment of the Bombay Stock Exchange in May of that year. Because the British administration was not concerned with the nation's economic development, the capital market was not well-organized and developed under their control. As a consequence, rather of turning to the Indian capital market for funding, many multinational corporations turned to the London capital market.

The size of the capital market remained minimal even after independence. The administration placed a strong focus on the growth of the agriculture sector and public sector enterprises throughout the first and second five-year plans. In terms of paid-up capital, public sector enterprises were stronger than private sector organisations, but their shares were not traded on stock markets. In addition, the timing, makeup, interest rates, price, allocation, and floatation fees of new issues were strictly monitored and managed by the Controller of Capital Issues. For approximately 45 years, many businesses were discouraged from going public due to these severe requirements.Speculators' go-to stocks in the 1950s were Century Textiles, Tata Steel, Bombay Dyeing, National Rayon, and Kohinoor Mills. As speculating increased, the stock market earned the monikersatta bazaar." Contrary to rumors, non-payment or defaults were not extremely common. In order to control stock markets, the government passed the Securities Contracts Act in 1956. Additionally, the Companies Act of 1956 was passed. The construction of a network for the growth of financial institutions and state financial organizations was another hallmark of the 1990s. -

War and drought in the nation throughout the 1960s contributed to negative tendencies. The 1969 restriction on forward trading and badla, which are formally known ascontracts for clearing,served to exacerbate these tendencies. Both borrowing money and carrying forward positions were made possible by Badla. Financial institutions, including LIC and GIC, were the most significant class of investors, which contributed to the revival of the mood. The Unit Trust of India, India's first mutual fund, was established in 1964. Badla commerce was restarted in the 1970s under the pretext of "hand-delivery contractsa group." The market was revitalized by this. On July 6, 1974, the government issued the Dividend Restriction Ordinance, which limited the payment of dividends by companies to 12% of the face value or a third of the profits of the companies that can be distributed as computed under 369 of the Companies Act, whichever was lower. This had a significant negative impact on the capital market. Due to this, the market capitalization of the BSE fell by almost 20% over night, and the stock market was closed for about a week.

When international corporations were compelled by FERA in 1973 to reduce their majority stakes in their Indian businesses in favor of the Indian people, the stock markets thereafter saw a boom. Many MNCs choose to avoid India. In four years, 1.8 million new shareholders were made possible by 123 MNCs offering shares worth Rs 150 crore. Shares of FERA were being offered at rates below what they were really worth. As a result, FERA dilution in India for the first time produced an equity cult. The FERA issues in large quantities were what really boosted the Indian stock market. Many investors finally had the chance to purchase shares of MNCs like Colgate and Hindustan Lever Limited. Then, in 1977, an unknown businessman named Dhirubhai Ambani began to access the capital market. Reliance Textiles, the company's ticker, continues to be a market leader and controls trade at all stock exchanges. In India, the securities market grew rapidly throughout the 1980s as a result of the abrupt discovery of attractive possibilities by millions of investors. Many investors made their initial forays into the stock markets. This boom was sparked by the government's liberalization initiative, which was started in the middle of the 1980s. Small investor participation, speculation, defaults, the banning of badla, and the restarting of badla all persisted. In the main market, convertible debentures were a common tool for resource mobilization. The primary market received a fresh lease of life with the introduction of public sector bonds and the successful mega issuance of Reliance Petrochemicals and Larsen & Toubro. The secondary market's volumes therefore increased as a result. The number of stock exchanges, publicly traded firms, paid-up capital, and market capitalization all rose throughout the 1980s.

The 1990s will be remembered as the Indian stock market's most significant decade. During this decade, new words like liberalization and globalization were created and aggressively popularized. In May 1992, the Capital Issues Act of 1947 was abolished. A new industrial policy, the emergence of the SEBI as the capital market's regulator, the arrival of foreign institutional investors, euro-issues, free pricing, new trading practices, new stock exchanges, the entry of new players like private sector mutual funds and private sector banks, and the boom and bust of the primary market were all features of the decade.There were significant stock market frauds throughout the 1990s. These caused the stock market to tremble and drove away small investors. One of the greatest frauds in the history of the capital market was the March 1992 securities scam, which included both brokers and bankers. Due to free pricing in the years that followed, many shady promoters who obtained funding from the capital market turned out to be fly-by-night businesses. The trust of the investors was damaged as a result. One such fraud, the M S Shoes case, which occurred in March 1995, forced a stop to fresh issue activities.

The securities fraud of 1991–1992 exposed the flaws and inefficiencies in the financial system. The swindle was what ignited the stock market reform. In terms of technology and market values, the Indian stock market saw a profound transformation. The trading method underwent significant modification thanks to technology. Two new stock exchanges the National Stock Exchange, founded in 1994, and the Over-the-Counter Exchange of India, founded in 1992put the Bombay Stock Exchange under national competition. For better clearing and settlement and dematerialized trading, the National Securities Clearing Corporation and the National Securities Depository Limited were established in April 1995 and November 1996, respectively. In 1995–1996 the Securities Contracts Act of 1956 was modified to allow for the trading of options. Additionally, rolling settlement was made available to all corporations' dematerialized segments in January 1998.

Participation in the stock market rose as a result of mechanization and geographic expansion. Information Technology stocks dominated the Indian stock exchanges in the late 1990s. Satyam, Wipro, and Infosys were some of these scrips. They were included in the 'new economy' scrips, which were popular at the time and included telecommunications and the media. In contrast to old economy firms that focused on assets, new economy firms were knowledge-intensive.

The Ketan Parekh scandal marked the beginning of the twenty-first century on the Indian capital market. As a consequence of this fraud, rolling settlement was implemented in all scrips starting in July 2001 and badla was abolished. Futures trading started in June 2000, and Internet trading was allowed in February 2000. The Unit Trust of India declared on July 2, 2001, that it would be stopping the sale and buyback of its popular US-64 plan owing to high redemption, which caused a panic on the stock exchanges. In 2003, the government decided to privatize the oil PSUs, which boosted stock prices.

Early in February 2002, VSNL, a prominent player in international telecommunications, underwent a significant divestiture. On the Indian stock exchanges, foreign institutional investors have become significant participants. In terms of volumes, NSE outpaces BSE, not only in the equities markets but also in the futures market. The Indian capital market has traveled a long distance. The capital market is now organized, reasonably developed, more international, and modernized. In terms of technology, the Indian equities market is among the finest in the world. Geographical borders are being destroyed and the investor class is expanding thanks to developments in computer and communications technologies that are coming together on the Internet. Online trade has spread around the world. Recently, Indian stock markets have begun to interact with international markets.

DISCUSSION

Free Pricing Regime in Primary Market

Under the terms of the Capital Issues Act of 1947, the Controller of Capital Issues used to oversee the new issues market before 1992. For the purpose of obtaining capital in the main market, businesses needed CCI permission. The controller determined the issue's time, quantity, and cost. Only par shares may be issued by new corporations, but shares at a premium might be issued by established companies with sizable reserves. This premium was calculated using a formula that the CCI had established. The net asset value and price earnings value are the two parameters on which the method is based. The issue price was set far lower than the share's current market value. Many problems were underpriced as a consequence of this set price approach.The Capital Issues Act of 1947 was abolished in 1992, and all restrictions on raising money from the market were also lifted. As a result, the promoters no longer need permission from any government in order to create the issue or set its price. The issue's price is decided jointly by the promoter and his merchant banker.

Companies, whether new or old, are allowed to choose the cost of their issuance. Under free pricing, a coalition of dishonest promoters and avaricious merchant bankers came to be. They published issues with optimistic but unfounded forecasts and offered shares for exorbitant fees. Prices fell as a result of these expectations not coming true. Additionally, businesses with a poor bottom line reissued rights at a premium on a regular basis. In the early stages of free pricing, issues of all types and premiums unheard of in business history were created. The major market was ruined by these problems. On the day they were listed at the stock market, the offer price for the majority of these issues was quoted. More than 3,000 of the 4,000 issues that were offered between 1992 and 1996 had their offer price stated on that day. Saurashtra Cements, for instance, debuted on the market in September 1993 for Rs 250 per share. When it was floated on the stock market, it was worth Rs 85; currently, it barely sells for Rs 8. In many instances, the free market devolved into a free-falling market. The regulator established standards for comprehensive disclosures for investor protection and imposed severe controls on merchant bankers, brokers, and other parties. Sadly, this wasn't done until after the tiny investors had left the market. Presently, promoters must provide a justification for the issue price in the prospectus and substantial disclosures about the risks in the offer document.

New Issue Mechanism

The fresh issue was governed by the Controller of Capital Issues until 1992. Offering the share at a set price was the mechanism used to determine the offer price under the CCI regime. In this case, the company and the merchant banker chose an offer price without considering the investor's input. Offerings at fixed prices were made to all investors. Furthermore, there was a significant delay between the date of pricing and the opening of the issue and the start of trading. This increased the likelihood of price changes throughout the interim. The idea that fixed price offerings cause high capital costs for businesses because shares are underpriced to draw interest is supported by empirical data.

In the period of free pricing, the price structure altered. Unrealistic and abrupt pricing structures during this time period sapped the stock market's luster. After burning their fingers on those premium issues, which are now being quoted at both their issue price and par value, investors withdrew from the market. The book building approach, a substitute for the capital market system's inefficient operation, is gradually gaining popularity in India. A method for determining an IPO offer price based on investor demand is called book building. The book building technique openly utilizes investor demand for shares at different values as a

significant input to arrive at an offer price, while the fixed price method does not take investors' desire into consideration. Book building is a recognized method of cash raising on a global scale. The US market was nearly completely created through book building in the 1940s and 1950s. The SEBI guidelines define book building as a process whereby a demand for the securities proposed to be issued by a corporate body is elicited and built-up, and the price for such securities is assessed to determine the quantity of such securities to be issued. This process may be accomplished through the use of a notice, circular, advertisement, document or information, memorandum, or offer document.In essence, the book building is a share auction. Investors may monitor the book being built on the NSE and the BSE, where a chart displays the bid price and the quantity of shares being sought. Book building simply implies that the "book is being built." This aids the investor in understanding market value. It gives investors the chance to place a group bid and utilizes the bid to determine a consensus price.

The Company initially names a book runner, sometimes known as a merchant banker. The book runner drafts the documentation, submits them to SEBI, and then receives an acknowledgment card. Shares will be sold by the issuer and book runner at a price that falls within a predetermined price range. Syndicate members, who include qualified brokers, merchant bankers, underwriters, financial institutions, mutual funds, and others, are asked to submit offers on the demand for securities at various price levels. The opening and closing dates for submissions should be included in the advertising. Normally, a bid is active for at least five working days. Together with the book runner and lead manager, the issuer determines a final cut-off rate and the final allocation based on the bids received. To prevent any potential takeover risks in the future, the issuer and book manager may put limits on the number of shares that may be allocated to each customer. Along with the procurement agreement, the completed prospectus is submitted with the Registrar of Companies. Only once the prospectus has been submitted to the ROC is the placement part available for subscription. One day before to the start of the public issue section, the placement portion closes.

The public section opens, and this portion has been allocated and listed. The cost established throughout the book-building process also applies to the public component. If the public component is oversubscribed, then a proportional allocation is made. If the public parts are not fully subscribed, the remaining amount is divided among those who choose placement. The amount of the public issue is increased if the placement part is undersubscribed. A red herring prospectus, which does not include information on the price, the number of shares being offered, or the amount of the issue, is submitted with the ROC for Book Building Issues. The underwriter strives to pique interest while gathering information from prospective buyers. A road show, so termed because the underwriter travels from city to city giving presentations on the firm and the offering, is a part of the procedure for gathering this data. A broker-analyst meeting, an investor meeting, and a news release are all ways that the road show is carried out. In book-built IPOs, the SEBI reinstituted the changing price band idea. The idea of a dynamic pricing band served as the foundation for the invention of book building in 1999. However, the SEBI switched to the idea of a set floor price in April 2000, which resulted in underpricing since the highest bids were placed at or slightly over the floor price. Depending on demand and the direction in which the book is being constructed, the range in a moving pricing band might go either upwards or downward. Either way, the band may be moved by 50%. Open and closed books are the two kinds of books that may be found in the Book building. The demand and bids are shown online during the bidding phase under the open book method of constructing. Both the NSE and the BSE terminals have access to this capability. This gives the investor the ability to track the quantity and movement of bids

throughout the time that the bid is available. In a closed book building, the book is not made public, so investors bid without knowing what other bidders' offers were. Thus, book building is the process of generating and building up demand for the planned issue, and determining the price at which the securities will be offered based on the bids received.

Advantages of Book Building Technique

Issuers may profit from price and demand discovery via book building. The process's goal is to presell the problem and eliminate any potential of under- or devolvement. Making public concerns requires less money and effort, and the processes are also made easier. Investors gain from the public offering because they can rely on the price at which the syndicate members bought the shares. As a result, it is unlikely that the price would decrease after listing.

Building Method's drawbacks

In contrast to the USA, where road meetings are conducted and the issue price is decided on a few hours before the issue opens, India's book building procedure is completely different. By providing two-way quotations on the secondary market, the lead manager creates a market for the paper until trading starts up. The Indian book-building method does not include any such clauses. Contrary to Western markets, the book-building process still depends on good confidence in India.

There are only a limited number of investors allowed to apply, and social pressure and reputation guarantee that there are no defaults. In India, there is little connection between businesses, merchant bankers, or investors, which is essential for book development. At crucial points in the book-building process, there is a lack of openness and there is no strict control. Issues may fail to elicit the appropriate public reaction because the price specified for both the public component and the placement portion is the same. It is not required to advertise book constructed problems to retail investors.

This raises the likelihood of negotiated agreements. It has not shown to be a reliable method of price discovery. Numerous issues have their issue price noted. The foundation of the price discovery method is the lag of more than 60 days between issue pricing and listing. Due to institutions' ability to collectively negotiate, issuers can be forced to sell at a discount. In the event of a bulk unloading, a high institutionalized holding may have an impact on the stock's liquidity and increase its volatility. The importance of small-scale investors in dictating price declines. Retail investors could also lack the knowledge necessary to assess the situation, making it difficult for them to choose the appropriate price.

Green Shoe Alternative

When the SEBI modified the rules in August 2003, it allowed the green-shoe option in book building issues. When referring to an option to allocate more shares than those offered in the public offering and to run a post-listing price stabilizing mechanism for no longer than 30 days, the term "green-shoe option" is used. This option is defined as follows:

1. If a firm wants to exercise the option, it must ask the general meeting for permission to assign more shares to the stabilizing agent at the conclusion of the stabilization term.
2. If necessary, the corporation should designate one of the merchant bankers or book runners as the SA in charge of the price stabilization procedure. Prior to submitting the offer document with SEBI, the SA should sign into an agreement with the issuing

firm that outlines all the terms and conditions pertaining to this option, as well as any costs or charges the SA would spend for this purpose.

3. The SA and the promoter who will lend their shares should also come to an agreement. The maximum number of shares that may be lent from the promoters or shareholders is to be specified in the agreement, and it should not exceed 15% of the entire issue size. The draft prospectus, draft Red Herring prospectus, Red Herring prospectus, and final prospectus must all include information on the agreements.
4. Promoters and pre-issue shareholders with more than 5% ownership of a firm, listed or unlisted, should lend the shares for the purpose of the green-shoe option.
5. These shares should be distributed to all applicants on a pro rata basis. After the exchange opens for trade, the stabilization mechanism should be provided accessible for no more than 30 days.

When the share price drops below the offer price, a stabilizing agent intervenes and purchases the shares off the market. He has the freedom to choose when, how many, and how much to purchase shares in order to maintain the post-listing price. The SA may acquire equity shares of the issuer from institutional shareholders or from the market, but not more than 15% of the issue size, in order to guarantee the post-listing price. To maintain the money and the shares for stabilization purposes, the issuer may establish a separate stabilizing fund account. The stabilizing action acts as a buffer against brief stock market volatility. After the start of the trading activity, the SA is also in charge of satisfying the surplus demand. When the stabilization period is finished, the issuing firm must distribute shares in dematerialized form to the amount of any deficit if the SA does not purchase from the market the excess shares that the business had overallocated. The ICICI Bank executed the first-ever green-shoe option exercise during a public offering.

The Life Insurance Corporation made history by being the first organization to lend shares on the open market. In order to guarantee the post-listing price, it gave 16 million shares to the DSP Merill Lynch. The green-shoe option is an investor protection mechanism, particularly for the post-listing period's protection of small investors. The underwriters gain from this option in both bullish and negative market scenarios. In a bull market, underwriters will choose a 15% extra allocation since the index is doing well. Underwriters will be able to increase their profits in this situation since the post-listing price will be automatically maintained and sometimes even go higher than the offer price. The underwriting option, however, may not be utilized in a bearish market, or the underwriters may purchase up to 15% of the market at a price lower than the issue price. The green-shoe option was formerly exclusively exercisable in book-built IPOs. It is now possible to execute IPOs. This action is anticipated to lessen volatility and boost investor confidence. An over-allotment option is another name for a green-shoe option. It is a method to provide an initial public offering post-Listing price stability. The term "green-shoe option" refers to an option that was initially issued by the Green-shoe Company. Red Herring Prospectus is a prospectus that lacks information on the price, the number of shares being offered, or the quantity of issuance.

IPOs

Through the electronic network of the stock exchanges, shares are issued online. The SEBI Guidelines, 2000 include a new section that includes the rules for online share issuance. According to the instructions, public issues may be submitted using either the online system or the current banking methods. The Companies Act of 1956's Sections 55-68A and the Disclosure and Investor Protection rules must be followed by the firm planning to make a public offering through the stock exchange's online system. The issuing corporation must engage into a contract with stock exchanges that have the necessary infrastructure for an

online offer, and it must designate brokers and registrars for the issue who can communicate electronically with stock exchanges.

This technique expedites the issuance process, and securities list within 15 days after the issue's conclusion, allowing for quicker access to money. According to the new regulations, securities must be allocated within 15 days of the issue's closing; otherwise, investors would be charged interest at a rate of 15%. Companies preparing an IPO may spend less on printing, stationery, and other expenditures. The approach avoids refunds except in cases of direct application, thus the investor also gains. The SEBI has released rules for the online offering of shares by corporations in an effort to put the Indian stock market on par with its international equivalents.

CONCLUSION

In conclusion, the capital market is a significant contributor to economic expansion by facilitating long-term financing and offering chances for investors to make investments. Maintaining investor trust and fostering sustainable economic growth depend heavily on its effective operation, which is supported by good regulatory frameworks and market openness. Policies that promote investor protection, market efficiency, and financial stability must be supported by policymakers. Businesses and investors must base their choices on thorough research and risk assessments.

The capital market can continue to play a crucial role in enabling capital flow, stimulating economic development, and improving financial well-being by seizing opportunities and overcoming obstacles. Global economic circumstances, geopolitical developments, and technology advances all have an effect on the stock market. For the capital market to be relevant and robust, constant adaptation to shifting market dynamics and innovations is required.

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CHAPTER 12

SECONDARY MARKET AND FOREIGN EXCHANGE MARKET

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ABSTRACT:

The secondary market and foreign exchange market are two critical components of the global financial system. This paper examines the functions, significance, and mechanisms of both markets. The secondary market enables the trading of existing financial instruments, such as stocks and bonds, among investors, fostering liquidity, price discovery, and efficient capital allocation. On the other hand, the foreign exchange market facilitates the exchange of different currencies, supporting international trade, investment, and hedging activities. The study delves into the role of technology, regulatory frameworks, and market participants in shaping the dynamics of these markets. Understanding the secondary market and foreign exchange market is essential for investors, businesses, and policymakers, as it enables informed decision-making and effective risk management in an increasingly interconnected and dynamic global economy.

KEYWORDS:

Certificate of Deposit, Commercial Paper, Interbank Market, Money Market, Mutual Funds.

INTRODUCTION

It is the first time a publicly unlisted firm offers to the public either a new issuance of shares, an offer to sell existing stocks, or both. In the event of an IPO, the information available on the company's historical performance and track record is often insufficient and may lack credibility. Due to this knowledge imbalance, moral hazard and adverse selection issues may arise. The SEBI has established strict entrance rules in order to empower investors to make educated choices and safeguard their interests[1], [2]. A follow-on public offering is when a firm that is already listed makes an offer to sell securities to the general public using an offer document. Investors who participate in these offers make educated choices based on its performance and track record. For organizations obtaining money via an IPO and an FPO, the SEBI has established qualifying requirements. The following are the entrance standards[3], [4]. The following standards must be met by the firm wishing to access the main market, according to:

Entry Norm I.

1. Net tangible assets with a minimum three-year holding period of Rs 3 crore, with no more than 50% kept in financial assets.
2. Distribute revenues from at least three of the five years before [5], [6].
3. A minimum three-year net worth of Rs. 1 crore.
4. If the company's name is changed, the new activity must have contributed at least 50% of the company's annual income [7], [8].
5. The issue size shouldn't be more than five times the net worth before the issue.

The SEBI has established two additional alternative pathways to a firm not satisfying any of the aforementioned standards in order to provide enough flexibility and to guarantee that real enterprises are not denied admission to the main market due to the rigor of the parameters. These are what they are: -

Entry Standard II:

1. The issue must follow a book-building procedure, with a mandatory minimum of 50% of the issue going to qualified institutional purchasers; otherwise, the investor's money will be reimbursed [9], [10].
2. There must be at least Rs. 10 crores in post-issue face value capital, or there must be mandatory market making for at least two years.

Entry Standard III

1. FIs and scheduled commercial banks engage in the "project" to the tune of 15%, of which at least 10% comes from the appraiser.
2. There must be a mandatory market making period of at least two years or the minimum post-issue face value capital must be Rs. 10 crores.
1. In addition to meeting the aforementioned qualifying requirements, the firm must additionally meet the requirement that at least 1000 potential allocators be included in its offering. The following entities are excluded from entrance standards according to the SEBI.
2. A firm engaged in infrastructure whose project has been evaluated by a PFI, IDFC, IL&FS, or a bank that was formerly a PFI and at least 5% of the project cost is funded by one of these organizations.
3. A listed company's rights issuance.

In other words, an initial public offering (IPO) is when a private business issues new securities, makes an offer to sell existing stocks, or does both. The IPO makes it possible to list and trade the issuer's securities. "Offer document" refers to the prospectus or offer for sale in the event of a public offering, and the letter of offer in the case of a rights offering. A public sector enterprise that has its shares listed on a recognized stock exchange is also considered a listed firm if it has any of its securities sold via an offer document published on that exchange. A company's current shareholders may offer its securities for sale to the general public via an offer document. A corporation may invite the general public to subscribe to the securities it is offering via a prospectus by issuing a public offering. A corporation that has submitted offer paperwork to the SEBI in order to issue securities is considered an issuer.

DISCUSSION

A market where current securities are resold or exchanged is known as the secondary market. The stock market is another name for this marketplace. The secondary market in India is made up of recognized stock exchanges that operate in accordance with laws, bylaws, and regulations that have been properly authorized by the government. Securities issued by the federal and state governments, public entities, and joint stock firms are exchanged on these stock exchanges, which make up an organized market. A stock exchange is defined as "anybody of persons, whether incorporated or not, constituted for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities" under the stocks Contracts Act of 1956. It trades in already-issued, already-existing, or already-outstanding securities. The main market mobilizes deposits and gives business units new or extra money.

Despite not directly adding to the availability of new capital, the secondary market indirectly does so by making securities issued on the primary market liquid. Stock exchanges are where this happens.

The Secondary Market's Purposes

1. To make the existing stock and debt securities more liquid and marketable.
2. To aid in economic expansion by allocating resources to the most effective use via the process of reinvestment after disinvestment.
3. To give a quick appraisal of securities due to internal environment changes. Such valuation makes it easier to estimate the micro level cost of capital and rate of return of economic units.
4. To safeguard the interests of investors by ensuring a level of safety and fair dealing.
5. To encourage businesses to perform better since investors can easily access the market price at the stock exchanges, which reflects performance.

Stock Market Scenario After Reform

The Indian secondary market presently has a three-tier structure thanks to the changes that were started in 1991:

1. Exchanges for regional stocks.
2. NASDAQ, or the National Stock Exchange.
3. The India Over Counter Exchange

In 1994, the NSE was established. It introduced new technology, trading techniques, institutions, and goods as the first modern stock exchange. The OTCEI was established in 1992 as a stock exchange that offered small and medium-sized businesses a way to raise money. There are now 23 stock exchanges in India, including the BSE, the NSE, the OTCEI, and the Interconnected Stock Exchange of India, in addition to 19 regional stock exchanges. A stock exchange among stock exchanges is the ICSE. Ahmedabad, Bangalore, Bhubaneswar, Kolkata, Cochin, Coimbatore, Delhi, Guwahati, Hyderabad, Indore, Jaipur, Kanpur, Ludhiana, Chennai, Mangalore, Pune, Patna, Rajkot, and Vadodara are the locations of the 19 regional stock exchanges. They follow the guidelines established by the laws and rules that have been authorized by the government and the SEBI.

Control Over Stock Exchanges

The Securities Contracts Act of 1956, which governs the recognition of stock exchanges, supervision of and control over recognized stock exchanges, regulation of securities contracts, listing of securities, transfer of securities, and many other related activities, governs the Indian stock markets. The Securities and Exchange Board of India was established in accordance with the Securities and Exchange Board of India Act, 1992, to safeguard the interests of investors in securities and to advance and oversee the securities market.

Organization, Management, and Stock Exchange Membership

A governing board made up of elected and nominal members oversees the operation of the regional stock exchanges. The exchanges are owned, controlled, and managed by the trading members who provide brokerage services. The governing board has broad authority to handle the exchange's funds and property, settle disputes, appoint office bearers' committees, admit and dismiss members, and oversee daily operations. The ownership and administration of the OTCEI and the NSE are distinct from the right to trade on the exchange since they are demutualized exchanges. Members of the stock market include brokers. Either on their own behalf or on behalf of customers, they make deals. The SEBI issues them a certificate of registration, and they are required to abide by the established code of conduct. Many brokers who formerly worked for proprietary and partnership businesses have now changed their status to corporate ones. To provide high-quality brokerage services, the NSE and the OTCEI

have both established stringent criteria for the admission of members. These criteria relate to capital sufficiency, track record, education experience, and other factors. Because they connect buyers and sellers and help with price discovery, brokers are crucial intermediates in the stock market. Brokers go into one of three categories: corporate, partnership, or proprietary. Most brokers in the older exchanges are proprietary in nature, while they are corporate members on the modern exchanges. Over the last several years, the Indian brokerage sector has seen a number of structural changes. In this sector, consolidation and restructuring have taken on a significant amount of significance. There were 9,129 brokers registered with the SEBI as of March 31, 2005. The CSE, followed by the NSE, the OTCEI, and the BSE, has the most brokers.

If a stock broker's yearly revenue does not exceed Rs 1 crore, he must pay a registration fee of Rs 5,000 per year. If it does, he must pay Rs. 5000 in addition to one tenth of one percent of any additional revenue. One billion. He is required to pay Rs 5,000 for a block of five financial years, starting five years from the date of first registration. Transaction fees are also assessed by the exchange. From broker to broker, the brokerage on trades varies. A maximum brokerage charge of 2.5% of the contract price may be assessed, excluding any applicable statutory fees such the SEBI turnover fee, service tax, and stamp duty. The brokerage sector is undergoing consolidation. Due to the large broking companies' monopoly over a significant portion of the broking industry, many brokerages are closing their doors.

Stock Exchange Demutualization

All Indian stock exchanges, with the exception of the NSE and the OTCEI, are owned and operated by brokers. In other words, the brokers who trade own and operate these exchanges as a group. Due to the brokers' ownership and management rights, there were often conflicts of interest where the brokers' interests prevailed over those of the investors. In the last several years, cases of price manipulation, recurrent payment problems on stock exchanges, and office holders abusing their positions of authority have all come to light. In order to maintain their integrity, rolling settlement and demutualization of stock exchanges were both announced. Any member-owned organization may demutualize and turn into a shareholder-owned business. Such a business might either be tightly owned by its shareholders or listed on a stock market. In India, stock exchanges are either associations of people or 25 corporations covered by the corporations Act. As a result, stock exchanges are not subject to taxes. A stock exchange changes from a non-profit organization to a profit-making and tax-paying firm via demutualization. On October 12, 2004, an ordinance amending the Securities Contracts Act became effective, requiring exchanges to become corporations and sever its broker members' links to the management. The legislation caps brokers' representation at 25% of the board of directors for stock exchanges. Additionally, it decreases their stake in the exchange from 100% to 49%. Moreover, other than stockholders with trading rights, 51% of an exchange's shareholding shall be owned by the general public. In every exchange, a broker's trading rights are separate from their ownership and management rights. Segregation is anticipated to increase stock exchange efficiency and transparency while protecting investors' interests.

The regulation also permits trading between brokers on different exchanges, which would help develop a trading platform for small and mid-cap firms. Stock exchanges are required by SEBI to divvy up their 51% shareholding in favor of the general public. In June 2007, the Bombay Stock Exchange completed the demutualization process. The government has approved a 49% foreign ownership limit on stock exchanges. For stock exchanges to expand and thrive and be competitive on a global scale, strategic investments are necessary. It is

anticipated that stock exchanges' mandatory corporatization and demutualization would improve their governance, prevent conflicts of interest, and safeguard investors.

Securities Listing

To make its securities tradeable, a company must list them on the exchange. Although a firm may apply to list on several stock exchanges, it is required to list on the regional stock market that is the closest to its registered office. A security that is listed on one exchange may be traded on another. The listing agreement contains clauses that aim to maintain market liquidity and investor safety. At the end of March 2007, there were 6000 securities listed on exchanges.If at least 10% of the stocks, subject to a minimum of 20 lakh securities, have been made available to the public for subscription, a company may apply for listing. Additionally, the issue is only made using the book-building process, with 60% of the issue size allotted to Qualified Institutional Buyers, and the amount of the net offer to the public is not less than Rs 100 crore. Alternately, a business must make at least 25% of its securities available to the public. For all exchanges, the fundamental standards for listing securities are the same. They are outlined in the listing agreement that was signed between the firm and the relevant exchange, and the exchanges keep an eye on their compliance. The primary source of revenue for the stock exchanges is the yearly listing fees levied on listed businesses. After a security is released to the public and listed on a stock exchange, the issuing company is required to provide the stock exchanges with ongoing disclosures about financial results, significant information that could affect the company's performance, and information in the form of a statement comparing actual fund usage and actual profitability to projected usage and projected profitability on a quarterly basis. The SEBI mandated that listed businesses provide their half-yearly results to the stock exchanges based on a restricted examination by their auditors or chartered accountants in order to increase transparency.

Center for Listing Authorities

The primary source of revenue for stock exchanges is the listing fees. The higher the listing costs, the more businesses are listed on an exchange. Exchanges are tempted to relax listing rules in order to get corporations to list. Additionally, listing specifications differ from exchange to exchange. As a consequence, issuers waste resources trying to meet the listing criteria of many exchanges at once. Therefore, there is a conflict of interest when stock exchanges control the businesses that provide them with money via listing fees. Given that stock exchanges are now in the process of being demutualized, this dispute might become worse soon.

With demutualization, stock exchanges' primary goal would be profiting maximization, which would further erode the listing conditions necessary to retain or raise listing fees. In order to address these problems, the nation needs a central listing authority that would be responsible for both establishing listing laws and monitoring compliance with those standards. In the UK, a listing body oversees the business while the London Stock Exchange handles trade. The establishment of a Central Listing Authority has been suggested by the government.

They would control prelisting practices, such as prospectus clearance. The Central Listing Authority was established by the SEBI with tight guidelines in order to make corporations more accountable for their conduct and stop any additional crises. When it comes to issues including the nomination of the CEO and supplying infrastructure and personnel to the CLA as needed, the SEBI offers operational and functional assistance to the CLA. Former Indian Chief Justice Shri M. N. Venkatachalaiah serves as the leader of the CLA. The CLA's goal is to provide uniform and consistent procedures for listing securities on stock exchanges.

Trading Contracts

An online screen-based electronic trading system has taken the role of the Open Outcry method, which was popular on regional stock exchanges a few years ago. Since its creation, the NSE and the OTCEI have used screen-based trading. Trading has moved from the floor to the broker's office, where deals are conducted using a computer terminal, since practically all exchanges have switched to electronic trading. There are 8000 terminals dispersed around the nation amongst all stock exchanges. A member of a screen-based trading system may input the quantity of securities and the prices at which he wishes to trade into the computer, and the transaction is carried out as soon as the computer discovers a matching order from a counter party. The open outcry method of the past has been replaced by the electronic trading system. As participants may see the whole market in real time, it guarantees transparency. By enabling the quicker absorption of price-sensitive information into the current pricing, it improves information efficiency and aids in effective price discovery.

With the removal of a network of brokers and jobbers and the resulting decrease in transaction costs, this also leads in increased operational efficiency. The depth and liquidity of the market have increased as a result of this system's ability to allow several players to trade concurrently with one another in complete anonymity from anywhere in the nation. As a result, many trading centers that are dispersed around the nation have been integrated into a single trading platform. The SEBI has approved the installation of trading terminals overseas and online trading. Now, investors from anywhere in the globe may place an order to trade Indian scrips online. Trading via the internet is more economical than doing it at a trading desk. Order-driven trading systems and quote-driven trading systems are the two categories of trading systems. In the order-driven method, orders are submitted into an electronic system from all over the nation and are continually matched without the assistance of a jobber or a market maker. Market makers that are eager to purchase and sell any amount are available in the quote-driven system and give two-way quotations that are constantly available in both directions. While the NSE only offers the order-driven method, the BSE offers both of these systems.

CONCLUSION

In conclusion, A vital component of the financial system, the secondary market and foreign currency market provide effective capital allocation, global commerce, and investment activity.

They provide up possibilities for managing risks, achieving financial objectives, and promoting economic development for investors, companies, and governments. Policymakers and regulators need to find a balance between promoting market innovation and preserving market integrity as the world's financial markets continue to change. To effectively traverse the intricacies of these dynamic and linked markets, investors and market players must exercise vigilance, keep informed, and use appropriate risk management strategies. Stakeholders may take advantage of prospects for economic development and success in the increasingly globalized world by comprehending and using the potential of these marketplaces. To avoid market manipulation, safeguard customers, and keep the foreign currency market stable, regulatory control is crucial.

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CHAPTER 13

EXAMINES THE ROLE OF TRADING RULES AND REGULATIONS

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ABSTRACT:

Trading rules and regulations are fundamental pillars of financial markets, governing the conduct of participants and ensuring fair, transparent, and orderly trading activities. This paper explores the importance and impact of trading rules and regulations in financial markets. It examines the role of regulatory bodies in setting and enforcing trading rules, as well as the key components of such regulations, including market structure, trading hours, price limits, and insider trading restrictions. The study also delves into the challenges and considerations in designing effective trading rules that strike a balance between promoting market efficiency, investor protection, and market integrity. Understanding trading rules and regulations is crucial for market participants, regulators, and policymakers, as it enables the establishment of robust financial markets that foster confidence, liquidity, and long-term stability.

KEYWORDS:

Margin Requirements, Market Manipulation, Minimum Tick, Order Types, Position Limits, Short Selling.

INTRODUCTION

In order to stop insider trading and unscrupulous trading activities, strict laws and regulations have been put in place. The exposure limit, intra-day trading limit, and margin system are all covered under the trading regulations. To control price volatility, brokers are charged a variety of margins, including daily margins, mark-to-market margins, ad hoc margins, and volatility margins. Depending on the exposures made by brokers in specific stocks, both on a proprietary basis and on behalf of customers, in relation to the total market exposure in the securities, stock exchanges impose various sorts of margins on brokers. Brokers pay some of these margins up front[1], [2]. These margins are gathered to stop traders from taking market positions that are larger than their purchasing power and are used to pay dues to the exchange, clearing company, and traders in the event that a broker runs out of funds[3], [4].

Depending on the amount of the positions taken in the market, the margins differ from operator to operator. With effect from 3 September 2001, the SEBI changed the margining system from a net basis to a gross one, and on 2 July 2001, it implemented a 99% value-at-risk based margin for all scrips under the mandatory rolling system. In a typical, daily market context, VaR assesses the worst anticipated possible loss resulting from an improbable bad occurrence. Before VaR, trading positions were solely recorded at book value and market fluctuations were not taken into account. This margin is maintained in a way that more than 95% of the time accounts for price changes. Sigma is often used for the measurement. No broker's trading volume may exceed the intraday trading limitations, often known as the volume limit. A broker must deposit more capital with the exchange if he wants to go beyond the limit. To maintain market safety, a broker's maximum gross exposure is set at 20 times his capital[5], [6]. In addition to these, there are standards for members' capital sufficiency, indemnity insurance, and exchanges' online position monitoring. Insider Trading Regulations, established by the SEBI to guarantee fair trading practices, prohibit insider trading and make

it a crime. There are currently distinct rules concerning purchases and takeovers in order to increase transparency of the takeover process and to safeguard the interests of minority shareholders[7], [8].

Breakers for Circuits

The SEBI adopted scrip wise daily circuit breakers price bands in 1995 to rein in excessive price volatility. If market prices change abnormally on either side, i.e., shift outside of a pre-specified band, the circuit breakers immediately halt/suspend trading for a certain duration. Circuit breakers do not stop trading, but if an order is beyond the permissible price range, it cannot be filled. Circuit breakers provide participants the opportunity to learn fresh information and evaluate the circumstance. This aids in calming anxiety. It aids exchange clearing houses in maintaining member surveillance. Circuit breakers, on the other hand, have caused pandemonium as players scramble to execute their orders before to an expected trading stop, especially during erratic swings[9], [10].

System for Trading and Settlement

The trade and settlement cycle were reduced from 14 days to 7 days as a result of the revisions. Securities were afterwards exchanged and resolved according to a standard weekly settlement cycle. In a trading cycle, positions were resolved by the payment of cash and delivery of assets after transactions had accumulated for a certain amount of time. The carry forward mechanism predominated at stock exchanges for a considerable amount of time since it enhanced trade volume and system liquidity. However, it also boosted speculation, which boosted price volatility and broker defaults and slowed down price discovery. So, a different approach known as rolling settlement was gradually established. The trading cycle for these assets is one day, and transactions are paid five days following the trade date under the T+5 basis rolling settlement method. Initiated in 10 scrips on a T+5 basis in January 2000, the rolling settlement system was then expanded to 153 more scrips in May 2000, 414 securities in July 2001, and all scrips afterwards. Since April 2002 and April 2003, the rolling settlement system has operated on a T+3 basis. Dematerialization and electronic financial transfer are necessary for the rolling settlement to be successfully implemented.

Removing Securities from Physical Form

An electronic book entry way of keeping and transferring securities has been proposed to address a number of issues, including theft, fake/forged transfers, transfer delays, and the paperwork involved with physical certificates. Investors may choose to hold securities in dematerialized or physical form.

The SEBI has required the mandatory settlement of trade in demat form in a few chosen scrips in order to hasten the dematerialization process. Only dematerialized securities from an initial public offering may be resolved. All IPOs will be released moving forward in a dematerialized format.

The National Securities Depository Limited and the Central Depository Service Limited are two depositories that provide dematerialized trading facilities. Over 99% of the turnover cleared by delivery is in a dematerialized form, and the dematerialization process is nearly complete.

Management of Risk

To encourage a secure and effective market, the stock exchanges have created a comprehensive risk management system under the direction of the SEBI. The establishment

of market surveillance systems, trade/settlement guarantee funds, trade/settlement guarantee funds to ensure timely settlements even if a member defaults to deliver securities or pay cash, and clearing corporations to guarantee financial settlement of all trades and reduce credit risk in the settlement system are all examples of actions taken by stock exchanges to reduce excessive volatility. The Clearing Corporation matches the transactions and oversees daily settlements as well as the reconciliation of sales and purchases. Additionally, it performs inspections and monitoring, manages risk for its members, and is accountable. Additionally, it analyzes members' net worth requirements and collects margins and capital from them. Its main responsibility is to ensure that every contract is carried out, either by acting as a counter-party to every transaction or by ensuring that every trade is performed. The establishment of this risk management system, which was lacking during the pre-reform era, is one of the major accomplishments of financial market reforms.

Web-Based Trading

In India, online trade started in April 2000. Investors may purchase and sell shares online using this method of trading. An investor must register with a broker providing online services before they can begin trading on the Internet. Along with opening a demat account with the broker, he must also create a bank account. The broker is in charge of his customers' risk management. Within the allocated limitations set by the broker to the customers, the orders are immediately entered into the trading platforms. The client order is sent to the broker's system for approval or rejection even if it exceeds the prescribed limitations. The settings may be changed by the broker online. His program enables the presentation of real-time market data, customer information, bank account administration, and transaction history.

As of March 31, 2006, 14.43 lakh investors have signed up to trade online. Volumes have significantly increased since the rolling settlement was implemented. The National Stock Exchange's internet trading volume increased from Rs 7288 crore in 2000–01 to Rs 1,83,428 crore in 2005–06.

During the years 2005–2006, about 11.68 percent of all trade volume was routed and carried out online. Online trading has significantly reduced transaction costs and improved an investor's liquidity choices, allowing him to buy or sell a stock whenever he wants. The investor has had access to a wealth of information through the Internet, enabling him to take measured risks.

Rolling Settlement Benefits

1. The rolling system's primary benefit over the badla method is its simplicity. The investors' exposure to risk and fraud was very high because of the badla system's lack of transparency and regulation. Since each company had an own settlement procedure, the investor had to maintain track of several equities. With rolling settlement, all scrips are resolved in the same manner on all trading screens, so the investor just has to keep track of the day of buy or sell.

2. By using this approach, arbitrage possibilities in scrips are eliminated.

3. Because the settlement procedure is standardized and players may concentrate more on market results, the price discovery process is improved.

4. This advancement in price discovery would result in a single, clearly defined price that various economic actors might use to process information.

5. Due to its transparency, it lowers settlement risk and minimizes the bid-ask spreads.

6. It promotes more participation since institutional investors who were previously prohibited from engaging in badla or netting trades during settlement may now do so because the technology reduces the time it takes for transactions to be settled.

7. It prevents price variations that occur around settlement dates. Rolling settlement lessens the working capital requirements for brokerage businesses with the establishment of clearing organizations.

8. It aids in lowering market volatility and turbulence by decreasing price manipulation and arbitrage.

9. Retail investors also gain since the time it takes to exchange assets for cash and vice versa is shortened.

United States Stock Exchange

The National Stock Exchange of India Limited was founded as a step toward professionalizing the capital market and to provide investors access to nationwide securities trading facilities. The NSE was established to provide investors with improved trading options and to harmonize the Indian financial markets with those of other countries.

Incorporation

With an equity capital of Rs. 25 crores, the National Stock Exchange of India was founded in November 1992. It was supported, among others, by IDBI, ICICI, LIC, GIC and its subsidiaries, commercial banks like State Bank of India and other organizations including SW Capital Markets Limited. NSE's key goals have been to support the capital market's professionalization process and to provide investors access to nationwide securities trading facilities.

NSE's primary goals are as follows:

1. To create a national trading platform for hybrids, debt instruments, and stocks.
2. To provide equitable access to investors throughout the nation via a suitable communication network.
3. To provide investors utilizing electronic trading systems a fair, effective, and transparent securities market.
4. To support book entry settlement systems and shorter settlement cycles.
5. To adhere to the most recent international securities market rules.

The NSE's formation is a crucial step toward improving investor trading options and bringing Indian financial markets into line with those of other countries. The screen-based trading method used by the NSE market is totally automated. India's secondary markets have mostly focused on equities trading. Government and corporate debt trading has not increased as much as it has in the equities markets. The NSE is anticipated to play a significant part in supplying the necessary infrastructure and trading capabilities to create a successful secondary market for both debt and equity products. The NSE is a stock exchange with a difference because, in addition to the traditional retail market for stocks, bonds, and other financial instruments traded on the capital market, it also operates the country's first screen-based trading facility for the wholesale debt market. The NSE is a new generation exchange, and it operates quite differently from traditional exchanges. Here are some examples of the main differences:

1. Trading at the NSE is computer-based, as opposed to trading on the floor at other exchanges.

2. Trades at the NSE are automatically matched with an order to sell something and a quantity that both parties agree upon.
3. System programming at NSE enables selection of the counter-party and setting of transaction size. However, such a decision may only be made negatively. For instance, it is possible to input blacklisted parties and specify the transaction size to prevent the purchase from being made in too many tiny lots or the opposite. Additionally, the validity of an order may be set as "good until day" or "good till cancelled." When the predetermined price is achieved, the computer will automatically execute the order after it has been established.
4. The buying/selling party keeps its counterpart's identity a secret. Due to the arrival of big players, speculative variants are prevented by anonymity.
5. Because the NSE does not have a trading floor, it is a genuinely national system.
6. NSE guarantees complete transparency since the price at which the trade is conducted is shown on the computer screen.

DISCUSSION

Trading System

The Exchange offers a screen-based trading option that includes automatic order matching. The system is based on orders and hides the identities of those involved in an order or a transaction. This makes it possible to place orders of any size without endangering the members' interests by disclosing their identities. Price time priority governs how the trading system functions. The system sorts all orders, giving the best priced order top priority for matching, such that the best purchase order matches the best sell order. The order that arrived first receives precedence over the one that arrived later in a group of orders with identical prices. Computers automatically match orders, maintaining the system's objectivity, fairness, and transparency. When an order does not match, it stays in the system and is visible to the whole market until a new order is received or the unsuccessful order is changed or cancelled. Regarding the types of orders that may be put on the system, the trading system offers users a great deal of freedom. An order may easily have a number of time-related, price-related, or volume-related conditions attached to it. The trading system also offers comprehensive market data online through a number of enquiry capabilities.

The market screens provide the member with comprehensive information at any moment on the entire order depth in a security, the best buys and sells accessible in the market, the volume traded in that security, the high price, the low price, the last traded price, etc. The member can make better selections thanks to the real-time updates to this information provided online. Thus, before placing orders, investors may be aware of the market's genuine position.

The status of the orders may also be known by investors nearly immediately after they are made with the Trading Members. In contrast to quote-driven trading, which is the norm at other exchanges, NSE uses order-driven trading.

As a result, genuine customer orders are used to conduct trades at NSE. A quotation-driven system, in contrast, allows brokers to provide a "buy quote" and a "sell quote" without taking into account the size of a specific transaction or the price that a customer is ready to accept. Even while this system's order-driven nature results in a slower pace between the purchasing and selling price, transaction execution speed may be slower when volume is low. Each trader at NSE gets a printout of all transactions, orders, and cancellations at the conclusion of each trading day, together with obligation reports outlining his position in both securities and funds.

Market for Debt in India

The debt market serves as the pivot of the modern financial system and is one of the most important elements of the financial system of any country. In the majority of industrialized nations, the debt market is far larger than the other financial markets, such as the equities market. The US bond market is the biggest securities market in the world, with a size of more than USD 13.5 trillion and a daily transaction of more than USD 500 billion. The size of the global bond market is close to USD 31.4 trillion, which is almost equal to the sum of the global GDP.According to current estimates, the entire size of the Indian debt market is between USD 92 billion and USD 100 billion. Indian GDP is accounted for by the debt market to the tune of 30%. In Asia, the Japanese and Korean bond markets are ahead of the Indian bond market in terms of estimated value of bonds outstanding. In terms of volume, the Indian debt market is bigger than the stock market. The debt and FX markets today command a volume of Rs 25,000 crore in terms of daily settled trades, compared to the meager Rs 1,200 crore in the equities markets. A very well-segmented debt market made up of the following has developed in the post-reform era:

1. The private market for business debt.
2. Bond market for public sector organizations.
3. Market for government securities.

More than 90% of the debt market's turnover is accounted for by the market for government securities. It makes up the main portion of the debt market.

Indian Debt Market's History

The Indian debt market has historically been a wholesale market, with participation limited to a select group of institutions, mostly banks. Due to regulatory requirements, banks made up the majority of market participants for government securities. Till the early 1990s, the debt market's turnover was also quite modest, at only a few hundred crores. Due to the managed interest rate regime and the availability of investment opportunities that provided investors with a greater rate of return, the debt market remained relatively undeveloped. The government required a sizable sum of money to spend in infrastructure and development projects towards the beginning of the 1990s. The government implemented reforms after realizing the need of a thriving, effective, and healthy debt market. The Reserve Bank made significant efforts to establish the public sector undertaking bond market and the private corporate debt market, although neither category has reached its full potential in terms of volume and liquidity. The debt market is essential for the effective mobilization and distribution of resources throughout the economy, for funding government development initiatives, for sending signals regarding the application of monetary policy, for facilitating liquidity management in line with both short- and long-term goals, and for setting prices in the financial markets for non-government securities. Debt markets are able to provide rewards according to risk, a choice of instruments to fit investors' preferences for risk and liquidity, higher safety, and reduced volatility. Consequently, there is a lot of room for future expansion in the debt market. A rising nation like India, which needs a lot of finance to expand its infrastructure and industrial base, depends heavily on the debt market.

Control of the Debt Market

While the corporate debt market is under the control of the SEBI, the government securities market and money market are governed by the RBI. The government published a notice on March 2, 2000 outlining the areas of responsibility between the Reserve Bank and the SEBI in order to encourage the orderly growth of the market. The RBI must control the sale and

acquisition of government securities, securities connected to gold, money market securities, and securities derived from these securities, as well as ready forward contracts in debt securities. However, if these contracts are executed on stock exchanges, SEBI must regulate them in accordance with the rules established by the RBI.

Features of the Debt Market

The following characteristics of a successful debt market include: -

1. The market structure is competitive.
2. Transaction costs are cheap in this market.
3. There is a lot of market participant variety and a secure market infrastructure.
4. A strong debt market lowers the cost of borrowing for the government.
5. By presenting more funding options, it aids in easing the demand on institutional finance.
6. It improves resource mobilization by releasing underperforming investments like gold and creating an S-curve.

Involved in the Debt Market

The fact that just a few big companies participate in the debt market has led to the development of the debt market into a wholesale market. While secondary market transactions are often handled over the phone, main debt issues are typically privately placed or auctioned to participants. A popular platform for dealing in debt instruments has evolved on the NSE Wholesale Debt Market Segment. The BSE just began trading in debt products. In the market for government securities, the major dealers serve as market makers. With the advent of new players including high net worth individuals, cooperative banks, big corporations, rids, and insurance firms, the debt market has grown more varied.

The following are the main players in the debt market: -

1. Federal and state governments:

To fund the budget deficit and other short- and long-term financial needs, the federal government issues dated securities and treasury bills. The government's investment banker, the Reserve Bank, is in charge of raising capital and issuing securities.

Municipalities, local governments, and other organizations also issue securities to cover their financial shortfalls and development initiatives.

2. Primary Dealers:

The Reserve Bank appoints these market makers, who have become prominent middlemen in the money market and market for government securities.

3. Public Sector Undertakings:

To fulfill their long-term and working capital requirements, they issue tax-free and taxable bonds. To save their extra cash, they also invest in debt instruments.

4. Corporations:

They participate in the debt market as investors and issuers.

5. Banks: These institutions are the market's captive investors in government securities. Both as arrangers and investors in the market for commercial paper as well as lenders and

borrowers in the call money market. They issue bonds to cover their long-term needs, and certificates of deposit to cover their short-term needs.

6. Mutual Funds:

The majority of investors in the debt market are mutual funds. They offer specialized debt funds, including gilt funds, money market mutual funds, and more. They have also become prominent dealers and players in the debt market. Foreign institutional investors are now able to purchase corporate bonds as well as government assets. Their investment is subject to certain restrictions.

8. Provident Funds:

PFs are significant holders of PSU bonds and government assets. They don't trade actively in their investments.

9. Chari Institutions and Trusts:

According to their bylaws, these entities are major investors in bonds and government securities. Additionally, they don't trade actively in their holdings. Another player in the debt market was satellite dealers, although the Reserve Bank stopped allowing them to trade as of May 2002.

The Negotiated Dealing System has taken the place of telephone-based system discussions in the market for government securities. The clearing and settlement mechanism in the market for government securities has undergone a transformation thanks to the Clearing Corporation of India Limited. Similar to how NSE transformed the equities market, both the NDS and the CCIL have drastically changed the debt market.

CONCLUSION

In conclusion, trading rules and regulations form the backbone of well-functioning financial markets. They provide the necessary framework for fair, efficient, and transparent trading activities, instilling investor confidence and attracting capital to the markets. Regulatory bodies must strike a delicate balance between investor protection and market efficiency while being agile in adapting to the ever-changing financial landscape. Market participants must also be aware of and comply with these rules to maintain market integrity and foster a healthy and resilient financial ecosystem. By continuously refining trading rules and regulations, policymakers and regulators can create an environment that fosters sustainable growth, innovation, and long-term stability in financial markets. Globalization and cross-border trading necessitate coordination among different regulatory authorities to ensure consistent and harmonized trading rules and regulations across jurisdictions.

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CHAPTER 14

A STUDY ONPROBLEMS OF THE DEBT MARKET

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ABSTRACT:

The debt market is a critical component of the financial system, allowing governments, corporations, and other entities to raise capital through the issuance and trading of debt securities. This paper examines the problems faced by the debt market, including issues related to liquidity, credit risk, interest rate volatility, and regulatory challenges. The study explores the implications of these problems on investors, borrowers, and the overall stability of the financial system. It also discusses potential solutions and policy measures to address these challenges and foster a more efficient, resilient, and transparent debt market. Understanding the problems of the debt market is essential for policymakers, investors, and market participants, as it enables informed decision-making and the formulation of effective strategies for managing risks and promoting sustainable debt market development.

KEYWORDS:

Bond Market, Corporate Bonds, Credit Rating, Debentures, Government Bonds, High-Yield Bonds.

INTRODUCTION

The lack of depth is the main issue plaguing the debt market among its many other issues. Banks are the largest debt holders. Banks are the largest and busiest actors in debt globally as well. However, banks are not authorized to trade in the secondary market and are only permitted to invest a very minimal amount in corporate debt in India. Additionally, the majority of banks retain government debt "ad nauseam" and are unable to sell it or make new investments owing to the degradation of its value. Furthermore, there hasn't been a purposeful effort made to create a secondary market for debt instruments, making it highly difficult for both people and corporations to acquire and sell debt on the secondary market. The lack of a central repository makes title and transfer into risky concerns, which exacerbates the situation. The debt market's growth has been greatly aided by the lack of ordinary investors[1], [2]. There is no reason why efforts to create a retail debt market won't be successful if the equities market can grab the attention of small investors. Unfortunately, there hasn't been any such organized attempt.

Even though the aforementioned issues are acknowledged to be significant, the lack of forward trading remains the debt market's most significant gap. Similar to the equities market, this would promote taking positions and the creation of complex instruments while also fostering the speculative breed that is so crucial for giving any market depth[3], [4]. The Indian debt market has suffered from excessive regulation, insufficient enforcement, and mistreatment at the hands of market participants. To get it to where it is now, there are a number of different factors, including these. The fraud has delayed the market's development by around five years, and it could still be some time before India experiences the birth of a thriving debt market. Despite the fact that reforms are moving in the right way, we cannot afford to disregard the enormous benefits that a mature debt market provides.TheDebt Market is the life line of the entire commercial activity of any country.

The debt market is the backbone of all commercial activity in any nation, making it a key indication of the economy's degree of growth. A well-functioning debt market is one that provides enough room for a range of instruments to fulfill the demands of various investor types and enough depth to absorb high trading volumes with little volatility in price. Treasury bills, promissory notes, bonds, debentures, mortgages, commercial paper, certificates of deposits, and UTI units are all examples of debt securities[5], [6]. They may have maturities between twelve hours and twenty years and can be both short-term and long-term. Government securities are excellent debt instruments with varying maturities that may be regarded as risk-free or zero-risk investments. India's debt market is divided into three categories:

1. Government securities.
2. PSU Bonds
3. Corporate debt instruments

Primary and secondary markets may be found in the debt market. Instead of investing, the majority of banks purchase government assets to satisfy their Statutory Liquidity Ratio requirements. In order to maintain a certain percentage of performing assets in their portfolio, several banks additionally invest in government securities over and above their SLR requirements[7], [8]. The absence of any organized exchange until recently has been a major factor in the secondary markets for debt instruments becoming obsolete. The primary gaps in the secondary markets are the lack of depth and liquidity in the majority of debt instruments, whether they are corporate or government-issued. Despite being founded in 1988 and 1993, respectively, the Discount and Finance House of India and the Securities Trading Corporation of India have not evolved into market makers. To establish a vibrant secondary debt market, the National Stock Exchange of India Ltd. launched a screen-based wholesale debt market sector. However, even this has not been successful, and while WDM volumes have been progressively rising, they have remained low for the last several months at roughly Rs. 1000 crore per month. The market for government securities has undergone two key modifications.

The government is switching from a system of low administered rates to one where rates on government securities are set by the market. Additionally, it would assist identify the real term structure of interest rates and develop a benchmark. The reserve requirement for banks is likewise being phased down. The government, in agreement with the RBI, also intends to prevent the budget deficit from spiraling out of hand. T-bills have been converted to dated securities by the RBI and the GOI. The RBI has recently implemented a number of initiatives to create a vibrant market for government securities. One step in this approach was the STCI's establishment; at the moment, only the RBI, DFHI, and STCI can be regarded as market makers. The RBI has, however, named six principal dealers for government securities. The secondary debt markets' liquidity would increase as a result. Transactions involving government securities are to be dematerialized via the subsidiary general ledger in order to increase transparency[9], [10].

Additionally, the delivery versus payment method will increase transaction security. In the two credit policy announcements, there have been no changes to the CRR or SLR rates. During 1995–1996 the federal government funded Rs. 19,000 crores via the rollover of securities that were about to mature and zero-coupon bonds.

Money Market and Capital Market Relationship

The connection between the money market and the capital market aids in illuminating the fundamental structure of the financial system. To create immediate cash flow or finance long-term initiatives, companies and government organizations may use sources of short- and

long-term funding within this framework. The way that money moves from savers to companies and the government to support operations and investment has a distinct impact on both markets. As a consequence, both markets provide investors chances to profit from hazardous endeavors and premiums.

Capital Market:

In general, the capital market is a venue where investments with maturities longer than a year may be traded. Investments made in the capital markets are primarily debt, equity, or derivative securities that are used to raise cash for long-term goals. For instance, in order to raise money, major firms sell equity instruments known as stocks. To establish long-term profitability and raise the company's worth, this money is reinvested in the business as equipment, real estate, or machinery.

Money Market:

The money market is the exchange where short-term securities with one-year or less remaining in their maturities are traded. Short-term bonds, or "money market securities," are often issued by governments or enterprises to finance short-term requirements. For instance, the federal government issues Treasury notes to investors in the United States and abroad in order to cover its budget deficits. Similar to this, big businesses issue commercial paper to attract investors and then utilize the money to pay for continuing operations.

Capital Market Objectives

Corporations and governments may borrow money from capital markets based on anticipated future cash flows. For instance, a large manufacturing business would borrow funds to update its gear by issuing bonds to investors. The renovation is predicted to boost output and revenue over existing levels. The rise in earnings enables the corporation to repay bondholders and raises the company's worth for stockholders. In order to cover the bond issuance and turn a profit for the firm, the corporation wagered that the rise in future revenue from the upgrade that was funded with bonds would be enough.

Applications for the Money Market:

Another option is to finance present operations rather than necessarily investing in them by using the money market. For instance, a huge corporation that lacks the funds to pay its workers may issue commercial paper to obtain cash. Investors utilize the money market as a safe haven for their capital since it offers higher returns than conventional savings or checking accounts while still allowing for even a little return on investment.

Risk

Long-term securities are exposed to higher levels of risk, while short-term assets have weaker correlations with risk. This happens as a result of long-term securities being exposed to the stock market's volatility for a much longer length of time. Short-term market volatility means that short-term assets are often less hazardous. Returns also correlate to this variation in risk. Returns on riskier assets are often greater than those on safer ones.

Market for Foreign Exchange

One of the crucial elements of the global financial system is the foreign currency market. The foreign exchange market is essential for converting currencies for short-term capital flows or long-term investments in the financial and physical assets of another country, particularly for economies in emerging nations. In addition to trade transactions, various financial receipts or

payments between nations requiring a foreign currency transaction also need the services of the foreign exchange markets. In emerging market economies, policies related to managing the currency rate, foreign exchange reserves, and external debt have attracted increased attention. There has been much discussion about the potential for currency rate flexibility, especially in light of the recent increase in reserves and rupee appreciation. On a daily basis, capital movements rather than the actual causes driving trade competitiveness have an increased impact on the exchange rate and interest rate arithmetic of the financial markets, necessitating a rigorous examination of the external debt position.

DISCUSSION

Concepts of foreign exchange:

Payments made to other nations using foreign currencies that a country owns are referred to as foreign exchange. It alludes to credit instruments that provide citizens of a nation a right to demand foreign currency. The term "foreign exchange mechanism" refers to the method for making international payments between two nations with different monetary systems. It is the process through which the local currency of a nation is changed into another currency. The values of several currencies from various nations must be connected in order to carry out international payments and transactions. Consequently, the ideas of foreign exchange and foreign exchange system were developed.

Exchange Rate Market

The term "foreign exchange market" describes the purchasing and selling of one national currency for another, i.e., the purchase of foreign currencies using domestic currencies and the sale of foreign currencies using domestic currencies. To fulfill their commitments overseas, import-export merchants change their international revenues into home currencies or home currencies into foreign currencies.

The foreign exchange market is made up of organizations that buy and sell different currencies, including the Treasury, Central Bank, foreign exchange institutions, etc.

Exchange Rate - Concepts

The rate of exchange is the rate at which two nations' currencies are transacted for one another. The worth or cost of a nation's currency in relation to other currencies is known as its rate of exchange.

For instance, the foreign exchange rate is $1 Rs. 40 if 1 US dollar is traded for 40 rupees. According to the credit instruments used in the transfer function, there are a number of exchange rates available on the foreign exchange market. The foreign exchange market primarily deals with the following two categories of exchange transaction:

1. **Spot rate:**

The price of foreign currency in terms of local currency payable for the currency's immediate delivery is referred to as the spot rate of exchange. The buyer will quickly receive payments in foreign currency from the seller, who must provide the currency on the spot.

2. **Forward Rate:**

A contract to purchase or sell foreign currency at an agreed-upon price at a future date is referred to as a forward rate. The forward rate is the planned price at which currency will be purchased and sold at a future time.

3. **Arbitrage:**

Using the disparities in exchange rates between two marketplaces, arbitrage is the act of purchasing a currency in one market and selling it in another in order to benefit. Two-point arbitrage is referred to when the arbitrage is limited to only two marketplaces. They are referred to as three-point or multi-point arbitrage if they cover three or more markets.

Foreign Exchange Market's Organization

In India, there is a three-tiered structure for the foreign exchange market, with the Reserve Bank at the top, Authorized Dealers that have been granted licenses by the Reserve Bank, and clients like exporters and importers, corporations, and other foreign exchange earners. Other than these major market participants, there are foreign exchange money changers who connect buyers and sellers but are not allowed to deal in foreign exchange on their own behalf. The ADs are governed by the rules established by the Foreign Exchange Dealers Association of India FEDAI. Dealings in the foreign exchange market include transactions between ADs and the exporters, importers, and other customers, transactions among ADs themselves, transactions with over one hundred customers, and transactions with over one thousand customers. There are now 92 banks that are known as Authorized dealers and are permitted to trade in foreign currency.

Larger Indian banks and the majority of international banks actively quote two-way rates among these. The banks do business directly or via the 47 foreign exchange brokers that are currently in operation. Institutions that provide term loans in addition to banks have been granted limited trading licenses. Foreign Exchange Dealers Association of India) establishes guidelines for determining commercial and other fees and gets involved in issues that affect ADs on a group basis. Spot and forward exchange contracts, as well as other derivatives, are freely traded on the market. Market efficiency and liquidity are often measured in terms of bid/offer spreads. Wider spreads are a sign of an unbalanced or illiquid market. In India, the typical spread for a spot market quotation is between 0.25 and 0.50 paisa, while the spread for a swap quote is between 1 and 2 paisa. Over time, there has been an increase in the overall turnover on the foreign currency market.

Indian Foreign Exchange Dealers Association

Due to the rapid expansion of international commerce, the RBI allowed numerous scheduled commercial banks to do foreign exchange business. With RBI clearance, the Foreign Exchange Dealers Association of India was established in 1958. For the purpose of doing foreign exchange transactions, each member bank must certify to RBI that it will follow by FEDAI's exchange rates and other rules and regulations. Since its incorporation on April 1st, 1990, FEDAI has been a registered business with a 20-member governing committee and chief executive. Its registered headquarters is in Mumbai, and local bankers are in charge of the committees in Delhi, Kolkota, Chennai, and Cochin. FEDAI develops a number of criteria for licensed dealers to follow while conducting foreign exchange transactions. Its main goal is to make sure authorized dealers are following RBI standards.

Players or Participants in the Foreign Exchange Market:

The various participant groups in the foreign currency market are as follows:

1) The country's foreign currency reserves are bought and sold by the central bank. Intervention occurs when the Central Bank consciously tries to affect the exchange rate between two currencies by purchasing one and selling the other.

2) Authorized Dealers:

In the foreign exchange market, authorized dealers who purchase and sell foreign currencies for profit include banks and non-bank entities. Since these vendors are in fierce rivalry with one another, the market is effective.

3) People & Businesses:

Foreign currency markets are used for commercial and investment activities by exporters, importers, foreign investors, multinational corporations, tourists, and other people.

4) Brokers:

Brokers connect foreign exchange buyers and sellers. They provide information on currency rates and are experts in currencies like the dollar and pound.

5) Speculators & Arbitragers:

Speculators and Arbitragers engage in both routine and speculative trading on the foreign currency market in an effort to benefit. They represent big banks when they act. Arbitragers are those who acquire foreign currency at a cheaper rate on one market and sell it at a higher one on another market.Credit instruments traded on the foreign exchange market include:

In the foreign exchange market, conversion is accomplished through a variety of instruments of credit in addition to the conversion of foreign currency notes and cash. These tools include:

1. Transfers through Telegraph

2. Letter Transfers

3. Checks and Drafts

4. Exchange bills.

Intervention by the RBI and exchange rate control

The RBI established its Exchange Control Department in 1939. The Foreign currency Regulation Act was created in 1947 in order to preserve the limited foreign currency reserves and manage them wisely. The statute gave the Central Government and the RBI the authority to oversee and monitor all transactions involving foreign currency. In the Indian foreign currency market, the RBI's primary goals are:

1) To ensure exchange rate stability.

2) To preserve limited foreign currency reserves for imperative uses.

3) To boost homegrown industries.

4) To encourage economic growth by limiting imports and promoting exports.

In 1973, the 1947 Fermat was expanded upon. This legislation went into effect on January 1st, 1974, and granted the RBI broad authority to manage the exchange control mechanism effectively.

Foreign Exchange Market and the role of the RBI

The regulations of FERA make clear the function that RBI plays in the foreign exchange market.

1) Administrative Authority:

The Central Government of India oversees the RBI, which is in charge of exchange control administration. Licenses for persons who engage in foreign currency trading may be issued by the RBI.

2) Designation of authorized dealers:

The RBI does not do business with the general public directly. It has named several authorized dealers. To function as authorized dealers in foreign currency, it has granted licenses to several commercial banks and "money exchangers." All foreign currency transactions must be conducted by them alone. The aforesaid clause is set down in FERA Section 3.

3. Issuing of instructions:

The RBI sometimes gives authorized dealers instructions regarding imports and exports, international money transfers, capital transfers, the transfer of investment income, etc. The 'Exchange Control Manual' has all of the instructions and guidelines provided by RB! once in a while.

4) Exchange rate fixation:

The RBI is in charge of determining the value of the domestic currency in relation to a basket of unspecified foreign currencies. All authorized dealers and money lenders are obligated to adhere exactly to this rate in all of their foreign currency operations. It is known as the official rate of exchange. The Foreign currency Regulation Ordinance of 1993 allows the RBI to express currency rates in terms of rupees per US dollar rather than US dollars per 100 rupees.

5) Regulating Import Trade:

Only legitimate permits are required for imports, and the RBI releases the required foreign currency. Only the reason for which it was received may be used to purchase foreign currency. According to FERA's requirements, only authorized dealers may accept payments for imports. The goods that may be imported without restriction are listed beneath. As a result, the RBI controls import commerce.

6) Export commerce Control:

The RBI regulates export commerce in coordination with customs officials and authorized dealers. Gold and jewelry exports are only permitted with a specific RBI permit. Only the authorised method recognized by the RBI may be used to collect payments for exports.

7) Managing International Travel:

International Travel is categorized as an unseen item. Through a suitable application, Indian citizens may get foreign currency from the RBI up to a certain amount for travel overseas. The foreign monies brought in must be reported at the entrance gate, and only authorized foreign exchange merchants may purchase them.

8) Controlling Foreign Investments:

Non-residents may only invest in India with the RBI's or the Central Government's prior approval. The Industrial Policy of the Government of India governs this. The RBI has recently allowed investments with and without repatriation facilities in a fairly lax manner.

Indian non-residents have access to excellent investment options. Foreign nations and citizens are also permitted to invest in Indian companies under more lenient conditions. FERA has been significantly loosened in order to promote exports and foreign investment. The most recent changes also allow Indian cash to leave the country via joint ventures overseas.

9) Import and export of gold, silver, currency notes:

The RBI has significantly loosened the restrictions on bringing in gold, silver money notes, etc. in recent years. The governing authorities must get notification of all imports. Accounts created and kept with authorized bankers in the names of people who live outside of India are referred to as non-resident external accounts. Under NRE accounts, several advantages are accessible, such as exemption from income tax, gift tax, wealth tax, etc.

Submission of Returns:

Authorized dealers are required to report to the RBI any foreign currency transactions they carry out.

This makes it possible for the RBJ to keep a close eye on Indian foreign currency transactions. In order to promote an active and efficient foreign currency market, the RBI acts as the apex bank and intervenes, monitors, and governs such markets.

Foreign Exchange Market Liberalization Measures Since 19991–1992

After 1991, the system exchange restrictions were loosened, and the RBI's involvement in the foreign currency market was restricted to preserving the rupee's exchange rate stability.

Dual Exchange Rate System

The government. In 1992–1993, the Government of India implemented the Liberalized Exchange Rate Management Systems, a dual exchange rate regime.

The government. of India acknowledged that there were two exchange rates in the nation: the official rate, which was regulated, and the market rate, which varies based on the state of the market.The following format was permitted for all transfers of foreign currency into India:

1) At a rate established by the free market, 60% of profits might be converted.
2) The remaining 40% of the profits must be sold via RBI-approved dealers at the official exchange rate. The government. It was thought that this would serve as a motivator to encourage exports. Between 1990–1991 and 1994–1995, the foreign currency reserves climbed from $5.8 billion to $25.2 billion.

Complete rupee convertibility on current accounts

Convertibility is the unrestricted ability to change local money into foreign currency for any reason.

The exporters and Indians living overseas were not delighted about giving up 40% of their profits at the official currency rate. So, the government. Since March 1993, a unified exchange rate system has replaced the dual exchange rate system.The government. Rupee convertibility on commercial accounts is permitted with no frills, i.e., Exporters and Indians living abroad may convert 100% of their foreign currency profits at market rates. Convertibility of the rupee on the current account was introduced by Dr. Man Mohan Singh, the then-Finance Minister. For all current commercial activities, such as travel, education, and medical costs, access to foreign currency was widened. As a result, the balance of payments situation improved and the amount of foreign exchange reserves rose.

Tara Pore Committee on Capital Account Convertibility

The ability to convert domestic financial assets into international financial assets is known as capital convertibility. The capacity of an Indian person to keep his money in dollars, purchase shares on the New York Stock Exchange, or own property overseas is known as full capital convertibility. For the Indian economy to be closely integrated with the global economy, full convertibility of the rupee is required both on the current account and capital account. According to the most recent signals, the RBI is hesitant to suggest complete convertibility since our financial system is still in its early stages of development and because it is still concerned about the abrupt outflow of money.

CONCLUSION

In conclusion, the problems faced by the debt market require proactive efforts from all stakeholders to foster a more resilient and efficient market environment. Policymakers and regulators must work collaboratively to design effective regulations that balance market stability, investor protection, and market innovation. Investors and market participants must be vigilant in managing risks and making informed decisions. By addressing these challenges and implementing appropriate solutions, the debt market can continue to play a crucial role in supporting economic growth, enabling capital raising, and contributing to the overall stability and development of the financial system. Simplifying and harmonizing regulations can improve market efficiency and reduce compliance burdens for market participants.Moreover, promoting transparency and disclosure standards can enhance investor confidence and foster a more liquid and well-functioning debt market.

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CHAPTER 15

IMPORTANCE OF FOREIGN EXCHANGE MANAGEMENT ACT

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ABSTRACT:

The Foreign Exchange Management Act (FEMA) is a crucial piece of legislation in India that governs foreign exchange transactions and regulates cross-border trade and investment. This paper explores the significance and objectives of FEMA, examining its key provisions and the role of the Reserve Bank of India (RBI) in its implementation. It delves into the importance of FEMA in promoting financial stability, safeguarding the value of the Indian rupee, and facilitating foreign trade and investment. The study also analyzes the challenges and opportunities in foreign exchange management under FEMA, including the need for effective enforcement and measures to address emerging global economic trends. Understanding FEMA is essential for businesses, investors, and policymakers, as it enables compliance with foreign exchange regulations and contributes to a resilient and dynamic Indian economy.

KEYWORDS:

Authorized Dealer, Capital Account, Current Account, DirectorateEnforcement, Export, Foreign Currency.

INTRODUCTION

The FERA was loosened, which fostered the expansion of multinational corporations in India as well as the influx of foreign money.

FEMA took over for FERA in 1999. While FEMA placed more of a focus on exchange administration, FERA placed more of an emphasis on exchange regulation or control. FEMA's mission is to support the orderly growth and upkeep of India's foreign exchange market while facilitating external commerce and payments. For the majority of the Act's rules, it was required to acquire RBI's consent under FERA.

No other clause in the FEMA requires receiving the RBI's consent, with the exception of clause 3, which deals with foreign currency transactions[1], [2]. Except in cases where explicit exceptions were provided, all transactions involving foreign exchange and non-residents were strictly forbidden under FERA. Non-residents are also not allowed to do any business in India.

Transactions involving foreign currency and international securities are the main focus of FEMA. While still present, restrictions on doing business with non-residents have been greatly reduced. Any individual who violates a FEMA 1998 requirement may be subject to a fine of up to double the amount involved in the violation. Unlike FERA, there would be no kind of incarceration as punishment. The regulations of FERA 1973 have been made simpler by FEMA 1998. The easing of foreign currency restrictions and the drive toward convertibility of capital accounts are the two main components of FEMA. Both import and export commerce as well as payment methods are governed by FEMA.

To promote international commerce, the limitations on currency withdrawals for current and capital account operations have been lifted[3], [4].

Exchange Rate and the Impact on Financial Flows

The progressive opening of current and capital account operations in the 1990s had a direct impact on the stability of the exchange rate, as did the growing amount of capital flows. There were sporadic moments of excessive capital inflows, which were followed by episodes of capital outflows ebbing, and then periods of capital inflows recovering. The 10-year period beginning in March 1993 might be split into three sub periods as described below from the perspective of analyzing the influence of external transactions on the exchange rate impact of external transaction on the exchange rate stability[5], [6].

April 1993 until August 1995

The Indian economy saw a rise in capital inflows during 1993–1994, 1994–1995 and the first part of 1995–1996 reflecting the high level of investor confidence. This, together with strong export growth, put upward pressure on the currency rate. The Reserve Bank absorbed the extra foreign currency supply in response to these inflows. In the process, throughout the lengthy period from March 1993 to August 1995, the nominal exchange rate of the rupee in relation to the US dollar stayed almost stable at roughly Rs 31.37 per US dollar[7], [8].

October 1995 to December 1996

During the months of September 1995 and February 1996, there were significant capital inflows. Real currency appreciation brought on by sharp increases in capital inflows upset market expectations and caused the rupee to depreciate in the second half of 1995–96, or between September 1995 and mid–January 1996. The Reserve Bank engaged in the market in reaction to the upheavals to demonstrate that the fundamentals were sound and to make sure that the inflated currency rate was corrected in an orderly and appropriate manner. To stop speculative assaults, monetary tightening encouraged the interventions in the FX market. These prompt and decisive actions stabilized the market, which persisted into the middle of January 1996. Another wave of unpredictability caused the Rupee to overshoot to Rs. 37.95 per US dollar in the first week of February 1996. The monetary and other measures were successful in restoring order, and from March to June 1996, the rupee fluctuated between Rs. 34 and 35 per US dollar. In the second half of 1996, the Rupee was range-bound. 1997 and later Since 1997, the foreign currency market has had to deal with a number of unfavorable internal and external events. The economic sanctions imposed after the nuclear testing in May 1998 and the border confrontation in May-June 1999 are two significant domestic events.

The external events included, among other things, the spillover from the 1997–1998 Russian and Asian financial crises as well as the steep rise in global petroleum prices from 1999, particularly from May 2000 onwards. Other external factors affecting the foreign exchange market include changes in interest rates in industrialized nations and fluctuations in the US dollar's value relative to other important world currencies. Due to the high level of uncertainty these changes caused, the merchant spot market gap increased from US $ 3.2 billion in 1997–1998 to US $ 4.4 billion in 1998–1999, reflecting the extra demand that resulted. In response, the Reserve Bank implemented timely monetary and other measures, such as changes to the Bank Rate, the Repo Rate, cash reserve requirements, refinancing to banks, surcharges on import finance, and minimum interest rates on past-due export bills, to reduce the destabilizing speculative activities during these episodes of volatility while allowing an orderly market. These measures were effective, and orderly conditions were quickly restored.Traditional financial instruments are financial instruments[9], [10].

The foundation of each company's financial structure is its equity share capital. The ownership interest or the interest of shareholders as determined by capital and reserves is

referred to as equity. Ordinary shares are sometimes referred to as "equities" since the word is also used to describe the limitless interest of ordinary shareholders. Large, medium, and small commercial companies all need cash to launch operations and maintain their operations.

Activities of Equity

1. In the majority of businesses, equity capital is primarily used to fund the acquisition of real estate, machinery, and equipment.
2. Its secondary purpose is to safeguard both long- and short-term creditors, who provide the company with funding.
3. Its third purpose is to act as a buffer to withstand any losses.

Financial Needs

For the following reasons, a commercial company needs cash or finance:

1. **Fixed Capital:**

Permanent financing, often known as long4erm. It is necessary to buy or produce fixed assets such as land, structures, factories or other types of buildings, equipment, tools, and accessories, as well as other types of durable assets like furniture and fixtures. In business, fixed capital denotes an investment that is made permanently. Initial fixed capital is often generated via equity investment and long-term loans for specialized financial organizations.

2. **Working Capital**

It is financing for the short term. It is necessary to finance ongoing production and marketing activities. It signifies current financing or current asset financing. A company needs enough cash flow to cover ongoing costs and short-term obligations. It guarantees a company's solvency and liquidity. Equity capital or ownership resources are also used to increase the minimal or standard operating capital. However, short-term borrowing in the form of bank credit and trade credit always covers supplemental and seasonal demands of current financing. A company must have enough cash on hand to cover its present obligations, as shown by fund-flow or cash-flow figures.

Financial resources for mergers, amalgamations, modernization, growth, etc. Every corporate organization has two basic goals: survival and development. Growth may occur via diversification, mergers, amalgamations, growth, etc. We need more stable internal sources of funding, mostly via share or debenture capital but also through retained earnings and depreciation. It is also possible to raise long-term loans from capital market institutions to fund growth. Many businesses have used retained earnings or self-financing to fund development.

Capital Types Capital is divided into four groups:

1. Equity Stocks

2. Favorite Shares

3.Debenture Capital

4. Reservations.

Debentures, bonds, and other credit instruments known as creditors' securities are often employed by businesses to obtain capital. Borrowed capital or debt capital is the term used to describe money raised via creditorship securities.

DISCUSSION

Debentures

Defined as a "document under the company's seal which provides for the payment of a principal sum and interest thereon at regular intervals and which is typically secured by a fixed or floating charge on the company's property or undertaking which acknowledges a loan to the company," a debenture is a legal obligation.

Debenture holders against shareholders

1. Share capital is owned money that comes from an outside source and is often not repayable over the life of the business. It is a permanent capital Debenture capital is a loan capital from an outside source that is typically repaid throughout the course of the company's existence, with a set maturity term of, say, 20 or 30 years.
2. The operator or owner of the company a registered member is a shareholder. The company's secured or unsecured creditor is the holder of the debenture.
3. Income Depending on the yearly net profits distributed, a shareholder may get a fixed or variable dividend. Only earnings that are retained or dispersed annually may be used to pay dividends. Debenture income is a set rate of interest that is less than the typical dividend rate. Regardless of the company's yearly earnings, interest must be paid, even when there are no profits.
4. Repayment not feasible unless the company is being wound up and the court confirms a specific resolution approving a capital reduction where shares are redeemable preference shares. May be paid off in accordance with the agreement or at the company's discretion. When the corporation defaults, they may become due automatically at the moment of winding up.

Manufacturers get support in the form of a supplier’s line of credit to encourage the sale of industrial equipment with delayed payment terms. Only genuine users of the equipment may utilize this credit facility for balancing, replacing, or modernizing needs. In accordance with this plan, a seller is given access to a non-revolving line of credit that must be used within a certain time frame. The only significant difference between this facility and the Bills Rediscounting Scheme is that in this instance, the supplier receives the payment directly from the financial institution, while in the prior example, a commercial bank acted as a middleman.

A new class of entrepreneurs is supported with seed capital assistance in order to spread ownership and management of industrial activities more widely. This unique program has been put in place to help entrepreneurs with their limited resources. In order to cover any shortfall in the necessary promoters' contribution, assistance is given in the form of interest-free loans. Depending on the number of application promoters, this aid is limited to between Rs. 15, lakhs and Rs. 40 lakhs per project.You may get money for equity and preference capital from the following sources:

Promotional quota:

1. Investments between corporations.

2. Promoters, filmmakers, pals, and family

3. International partners.

4. Nations in development that export oil.

5. Corporations for State Industrial Development.

6. Shareholders of the firms that promote.

7. Accruals made inside.

8. Issue of rights to current shareholders.

Quota for non-promoters:

1. A general concern among Indian citizens.

2. Public issuance on a repatriable and non-repatriable basis to non-residents of Indian descent,

Listed public companies and public sector corporations may raise debtor capital funds in the form of secured convertible or non-convertible debentures with the aim of funding any expansion or diversification project or to increase the long-term resources of the company for working capital needs. A maximum of 20% of the total current assets, loans, and advances may be issued in debentures to finance working capital needs. On the basis of the financial institutions' and the MRTP Commission's approval of the financing plan, the issuance of debentures for project financing is taken into consideration. After taking into account the planned debenture issuance, the debt-equity ratio shouldn't typically be more than 2:1. For projects requiring a lot of cash, this standard is reduced. To be eligible to issue debentures, a company's shares must have been listed on one or more stock exchanges and the market quotation of those shares must have been above par for at least six months prior to the date the application for authorization to do so was submitted to the Controller of Capital Issues.

Securities Underwriting

Underwriting significantly aids in the marketing of securities. According to the definition of an underwriting agreement, it is "an agreement entered into before the shares are brought before the public that in the event that the public does not take up the entire amount specified in the agreement, or the number specified therein, the underwriter will, for an agreed commission, take an allotment of such portion of the shares as the public has not applied for."

Benefits and Importance of Underwriting

A public company must obtain "minimum subscription" within 120 days of the prospectus' release in order to allocate shares, and without a declaration that the required minimum subscription was received, the company will not be granted a certificate from the Registrar of Companies allowing it to conduct business. Underwriters are very helpful in ensuring that the firm raises the necessary share capital. Thus, underwriting is crucial to the growth of the capital market and promoting industrial development. It should be noted that one of the key elements in the development of the Indian capital market in the years after independence was the expansion of the underwriting industry. The amount covered as a proportion of all private capital offerings made available to the public ranged from 72% to 97% during the last 10 years. Thanks to commercial banks, brokers, and public financial firms, the underwriting industry has seen spectacular growth. Brokers are now taking on underwriting risks in the new issues market since forward trading was abolished.The corporate sector benefits from the underwriting industry in the following ways:

The danger of not being able to find purchasers for all of the issues issued to the public is removed through underwriting. As a result, the corporation may be rather certain that it will raise enough share capital. Additionally, underwriters said the business in adhering to legal requirements, such as obtaining the required minimum subscription within the allotted time. The highly specialized task of distributing securities is relieved from the issuer by

underwriters. Because they are knowledgeable about the capital market circumstances, underwriters may provide the firm with specialized advice on the timing of security issuance, the number and kind of securities to be issued, the potential offering price, etc. Because reputable underwriters' underwriting of issues increases public trust, the underwriting industry aids in boosting capital market money mobilization.Conditions on the financial markets are stabilized by underwriters' actions.

India has seen a growth in professional underwriting, especially after the establishment of ICICI. The development of the promotional underwriting service was greatly aided by the ICICI. However, underwriting has been growing in the nation, especially since the founding of the ICICI in 1955. Commercial banks, investment businesses, stock brokers, and public sector financial institutions including the IFC, ICC, IDBI, SFCs, UTI, and LIC have all contributed significantly to the development of the underwriting service. Stock market brokers started taking up underwriting risks in the new offerings once forward trading was abolished. According to statistics for the most recent period, the amount underwritten as a proportion of all private capital issuance made available to the public ranged from 72% to 97%.

Insurance Companies

The following are some of the significant underwriting companies in India:organizations in the Finance Sector: Public sector industrial finance organizations including the IFCI, IDBI, ICICI, LIC, and UTI provide considerable underwriting assistance.

Commercial Banks:

In recent months, commercial banks have shaken off their reputation for conservatism and adopted a more positive outlook on underwriting. Despite a large increase, commercial banks' underwriting activity still only makes up a relatively tiny portion of the overall underwriting market.

Investment firms:

The investment firms, which are mostly marketed by major corporate houses, have been crucial in the development of the underwriting industry, particularly in the early stages.

Stock Brokers:

A number of significant stock brokerage companies have also been heavily involved in the underwriting industry. However, broker companies have been operating their underwriting division as a side business.

Bond Market Concept

A bond is a kind of debt instrument used in finance, where the authorized issuer owes the bondholders money and, depending on the bond's conditions, is required to pay interest and/or refund the principal at the bond's maturity. A bond is a legally binding agreement to pay back borrowed funds with interest at predetermined periods. A bond is thus similar to a loan in that the issuer acts as the borrower, the holder as the lender, and the coupon acts as interest. With the help of bonds, the borrower may finance long-term investments or, in the case of government bonds, current expenses. Commercial paper and certificates of deposit are both regarded as money market tools, not bonds. Bonds must be repaid over a certain length of time at regular intervals. Although both stocks and bonds are considered securities, shareholders have an equity ownership in the corporation, whereas bondholders have a

creditor stake. Another distinction is that stocks may remain outstanding forever, but bonds typically have a limited period, or maturity, after which the bond is repaid.

A console bond, which is a perpetual bond, is an exception. Public bodies, financial institutions, businesses, and supranational organisations all issue bonds in the main markets. Bonds are most often issued via the underwriting procedure. In underwriting, a syndicate of securities companies or banks purchases the full issue of bonds from the issuer and then resells them to investors. The risk that it won't be able to sell the issue to end investors is assumed by the security company. Book runners coordinate the bond issue, maintain direct communication with investors, and serve as the bond issuer's counsel with regard to the time and cost of the bond issue. Before opening books on a bond offering, the book runners' desire to underwrite must be considered since there may be little interest in doing so.Government bonds are often issued via auctions, when both the general public and banks may place bids. The price is not set, but the coupon is, therefore the return percentage depends on both the price and the coupon.

Bond features include:

The most crucial characteristics of a bond are:

1. The amount on which the issuer pays interest and which, most often, must be returned at maturity is known as the nominal, principle, or face amount. A redemption amount for certain structured bonds may be different from the face value and may be based on the performance of specific assets, such as a stock or commodities index, a foreign exchange rate, or a fund. Due to this, an investor may get less or more at maturity than his initial investment.

2. Bonds are first purchased by investors at a price known as the "issue price," which is normally equal to the nominal amount. Thus, the issue price minus issuing costs constitutes the issuer's net proceeds.

3. The issuer must pay back the nominal amount by the maturity date. After the bond's maturity date, the issuer is no longer obligated to the bondholders as long as all payments have been fulfilled. The term, tenor, or maturity of a bond are all terms used to describe how much time remains until the maturity date. Although debt securities having a duration of less than a year are often referred to as money market instruments rather than bonds, the maturity may be any amount of time.

The period of the majority of bonds is up to thirty years. There have been bonds issued with durations of up to 100 years, and some even have no maturity period. Early in 2005, a market for bonds with a fifty-year maturity started to emerge in euros. searching for U.S. There are three categories of bond maturities for Treasury securities:

a. Maturities up to one year, or short term;

b. Maturities in the medium term: one to 10 years;

c. longer maturities are those of more than 10 years.

4. The interest rate that the bond issuer pays to bondholders is known as the coupon. Typically, this rate is constant throughout the duration of the bond. It may also change in relation to a money market index, like LIBOR, or it may take on more stranger forms. The term "coupon" derives from the fact that tangible bonds with coupons attached were formerly issued. Bond holders would exchange their coupons for interest payments from banks on coupon days.

Bond Types

The descriptions that follow are not mutually exclusive, and a connection may fit into more than one category.

1. Bonds with fixed rates have a coupon that doesn't change during their lifespan.
2. A variable coupon on floating rate notes is connected to a benchmark interest rate, such as LIBOR or Euribor. For instance, the coupon may be specified at three-month US Dollar LIBOR plus 0.20 percent. The coupon rate is updated on a regular basis, usually every one to three months.
3. Zero-coupon bonds do not accrue interest over time. The interest is essentially rolled up to maturity since they are issued at a significant discount to par value. On the day of redemption, the bondholder gets their whole principal back. The U.S. government's Series E savings bonds are an example of zero-coupon bonds. A financial firm may make zero-coupon bonds from fixed-rate bonds by "stripping off" the coupons from the principal. In other words, the bond's ultimate principal payment and the divided coupons may both be exchanged independently. Look up IO and PO.
4. Bonds with an index to inflation where both the principal and interest payments are made. Generally speaking, the interest rate is lower than fixed rate bonds of equivalent maturity. However, the payments rise in line with inflation as the principal amount rises. In the 1980s, the first sovereign issuer to offer inflation-linked Gilts was the United Kingdom. Examples of inflation-linked bonds issued by the U.S. government are Treasury Inflation-Protected Securities and I-bonds.
5. Additional indexed bonds include equity-linked notes, bonds indexed on a business indicator, and bonds indexed on a nation's GDP.
6. Bonds known as asset-backed securities have underlying cash flows from other assets that support their interest and principal payments. Mortgage-backed securities, collateralized mortgage obligations, and collateralized debt obligations are a few examples of asset-backed securities.
7. Bonds that are subordinated to other bonds of the issuer in the event of liquidation have a lower priority. There is a hierarchy of creditors in a bankruptcy. The liquidator is paid first, followed by taxes to the government, etc. The holders of what are known as senior bonds are first in line to receive payment. The holders of subordinated bonds are compensated after their payment. The danger is thereby increased. As a result, senior bonds often have a higher credit rating than subordinated bonds. Asset-backed securities and bank-issued bonds are the two primary types of subordinated bonds. The latter are often released in phases. The senior tranches are repaid first, followed by the subordinated tranches.
8. The terms perpetuities or Perps are other names for perpetual bonds. They are not yet of maturity. The most well-known of them are the UK Consoles, sometimes referred to as Undated Treasuries or Treasury Annuities. Even though the quantities are now minuscule, several of them that were first produced in 1888 are still in circulation. From a financial perspective, certain ultra-long-term bonds are practically perpetual since the principal value is now very low.
9. A bearer bond is a legal document that has no designated holder. In other words, the bond's value may be claimed by the owner of the paper certificate. They are often identified by a number to avoid counterfeiting, although they may still be exchanged like currency. Bearer bonds carry a high level of risk since they might be stolen or lost. Bearer bonds were seen as a way to hide income or assets, particularly when the United States implemented federal income tax. In the 1960s, American firms ceased

issuing bearer bonds. State and municipal tax-exempt bearer bonds were outlawed in 1983 after Treasury ceased issuing them in 1982.

CONCLUSION

In conclusion, A key piece of law that has been essential in advancing international commerce, foreign investment, and financial stability in India is the Foreign Exchange Management Act (FEMA). Under the direction of the Reserve Bank of India, it was successfully implemented, which helped the nation's economy expand and become more integrated into the world economy. FEMA can continue to promote a thriving and robust foreign exchange market, maintaining India's position as a vital participant in the global economic arena, by continuously addressing new problems and possibilities. For companies and investors looking to take advantage of India's expanding international trade and investment scene, observing FEMA's regulations and keeping up with regulatory revisions are essential. To keep FEMA current, effective, and in line with the changing economic situation, the government and regulatory bodies must regularly evaluate and amend it. For companies and investors involved in foreign currency operations, increased knowledge of and education about FEMA's laws and compliance requirements is crucial.

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CHAPTER 16

PUBLIC SECTOR UNDERTAKING BOND MARKET

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ABSTRACT:

The public sector undertaking (PSU) bond market is an essential segment of the Indian debt market, catering to the borrowing needs of various government-owned entities. This paper explores the significance and dynamics of the PSU bond market, examining its role in financing infrastructure projects, supporting public sector enterprises, and diversifying investment options for investors. It delves into the challenges and opportunities faced by the PSU bond market, including credit risk, liquidity concerns, and regulatory considerations. The study also analyzes the impact of government policies and market reforms on the development of this market. Understanding the PSU bond market is essential for policymakers, investors, and market participants, as it enables informed decision-making and effective risk management in the context of India's evolving economic landscape.

KEYWORDS:

Bond Market, Corporate Bonds, Credit Rating, Debt Securities, Government, Infrastructure Bonds.

INTRODUCTION

Medium- and long-term obligations are known as public sector undertaking bonds and are issued by public companies. When the central government discontinued or curtailed financing to PSUs via the general budget in the late 1980s, the problem of PSU bonds emerged. To raise money, PSUs issue bonds on the main market. PSUs issue bonds to raise money from the market to cover their recurring needs for working capital or capital expenditures. Over the last ten years, the market for PSU bonds has significantly expanded. All PSU bonds have an imbedded put or call option, and some of them also have a bullet redemption. These are often issued by businesses involved with infrastructure, such railroads and electricity corporations, and the issue amounts range significantly from Rs. 10 to 1,000 crores[1], [2]. The maturities of PSU bonds range from five to 10 years. Each one is issued in the denomination of Rs 1000.PSU bonds are often privately arranged with banks or significant investors. Rating is not required for privately issued issues, but it is for publicly traded securities, which must be rated by one or more of India's four rating agencies. In the past, PSU bonds have never defaulted, and PSUs have a reputation for being almost sovereign entities. State governments often guarantee the interest and principal payments on bonds issued by state-owned PSUs. These assurances are provided primarily to aid in the fund-raising efforts for several infrastructure projects with a protracted gestation period[3], [4].

Tax-free and taxable bonds are the two kinds of bonds that PSUs may issue. Bonds that are tax-free are those whose interest payments are not included in the investor's income. PSUs raise money for such projects by issuing tax-free bonds or bonds that qualify for certain Income Tax Act exemptions, with previous government permission via the Central Board of Direct Taxes[5], [6]. Central PSUs like MTNL and NTPC, as well as state entities like the State Electricity Boards and State Financial Corporations, have generated money by issuing tax-free bonds. SLR is available on the bonds issued by the State Financial Corporations to cooperative banks and non-banking finance firms. These bonds' interest is computed either

daily or every 365 days. It's appropriate to deduct taxes at the source. Prior to 1991, when the pre-reform era began, the maximum interest rate on taxable bonds was set at 14%, while the maximum interest rate on tax-free bonds was set at 10%. The maximum amount that banks may invest in PSU bonds was 1.5% of additional deposits. After the restriction on PSU bond interest rates was repealed with effect in August 1991, various PSUs launched bonds at interest rates between 17 and 18 percent. The cap on tax-free bonds was later increased to 10.5%. Additionally, the cap on bank investments in PSU bonds was eliminated, allowing for unlimited investment[7], [8].

Initially, provident funds were permitted to purchase PSU bonds with 15% of their additional deposits. Later, the percentage was raised to 30%. In October 1993, new regulations for the issuance of PSU bonds were released. According to the rules, taxable bonds must have a minimum duration of seven years, although tax-free bonds may have whatever maturity that PSUs choose. The public issues must adhere to the rules set out by SEBI. PSUs are permitted to issue a range of bonds, including deep discount bonds and variable rate bonds. A stock exchange must list all new offerings. Banks, insurance companies, non-banking financing firms, Provident funds, mutual funds, financial organizations, and individuals are among the investors in PSU bonds[9], [10]. Since the limit on taxable bond interest rates was eliminated in 1991–1992, taxable bonds have grown in popularity. PSU bonds, which had previously been floated on the public issue market, were privately placed in the 1990s.

For the issuance of bonds, the PSUs opted the private placement approach. Since 1997–1998 they have not engaged the main market. PSUs prefer the private placement approach since there is no active secondary market for PSU bonds. Additionally, using this method to generate money is simpler and less expensive. For their financial needs, the PSUs kept using the private placement market.PSU bonds are often issued and exchanged on the secondary market in the form of stock certificates or promissory notes. While stock certificates may only be transferred by a properly completed transfer deed and are subject to stamp duty unless explicitly excluded, promissory notes can be transferred by endorsement and delivery. Settlement and clearing are now done on a recognized form. PSU bonds are free from stamp duty since they don't need a transfer document to register a change in ownership. However, contract notes for PSU bond transactions incur a 0.01 percent stamp tax.

If PSU bonds are in demat form, repos are permissible. PSU bonds are traded on the WDM section of the NSE and debt segment of the BSE; stamp tax on transfer of dematerialized instruments was repealed as part of the Union Budget for 1999–2000's effort to promote secondary market activity. PSU bonds have a low level of liquidity, while having a greater level than state or federally guaranteed bonds. Brokers are used for the majority of deals. PSU bonds have lower brokerage fees and bid-offer spreads than state government and government-guaranteed bonds. For state-run pension funds and other financial institutions, trading occurs in multiples of Rs 5 lakh, whereas for small trusts and ordinary investors, trading occurs in multiples of Rs 1,000,000. The average daily trading volume is Rs. 5 crores, while the average transaction value is Rs. 2 crores.

PSU bonds had a higher yield in the beginning of the 1990s. As a result, commercial banks, mutual funds, and other PSUs with plenty of capital made investments in these bonds. In the early 1990s, they were one of the most popular instruments. The market employed "tax stripping repo strategies" to arbitrage tax differentials, which led to the tax-free bonds being the most popular. Due to the fact that money was stolen from the banking system via this market during the Securities Scam of 1992, it was heavily abused. When PSU bond offerings were more significantly deregulated in 1993, this market began to recover. As a result, institutional participation in this market area significantly increased. Since 2000–01, there is

no question that the volume traded has climbed, but the percentage share of the overall volume traded has fallen. The majority of PSU bonds are privately put, which lowers the amount of floating stock and results in the low level of activity. Because individual investors are not engaged in trading and there are no established rules, the level of activity has not increased more quickly. To increase transparency and liquidity in this market sector, standard rules and market procedures should be established. In the PSU bond market, a main dealer system comparable to the government securities market may be implemented. This will improve secondary market trading and liquidity, which will support the expansion of the PSU bond market.

Innovative Financial Instruments

In the 1990s, the Indian financial system underwent a considerable shift. Some of the significant reforms that have altered the Indian financial system's landscape include the deregulation of lending rates, free pricing of equity issues, admission of institutional investors from the private sector, including foreign investors, opening up of the banking sector to the private sector, enabling Indian companies to access foreign capital markets directly, and others. The business sector now faces more competition because to this newly discovered independence. The capital market is a crucial resource for satisfying the expanding long-term needs of corporations in both the public and private sectors. The battle among the different classes of issuers for a piece of the investors' money has become fierce as a result of the enormous fund needs of both corporate and financial institutions, but on the other hand, investors are proving to be more discerning and astute. Therefore, it has become crucial for issuers to develop and construct new financial products in order to satisfy the disparate needs of both. These advances, which have completely changed the way business is conducted, were made possible by financial engineering.

DISCUSSION

New Financial Instrument

When compared to the characteristics of already existing instruments, a new financial instrument may include some new terms of agreement features. Very few financial products are brand-new creations. Many are just brand-new features that have been added to traditional financial instruments. Equity shares, preference shares, and debentures partially convertible, fully convertible, and non-convertible are examples of common financial instruments. A conventional instrument becomes a novel instrument when certain additional features, such as attaching a warrant to the non-convertible component of a debenture, are introduced.

Causes of Financial Instrument Innovations:

1. Each product requires ongoing reengineering. Additionally, it has to be customized to meet the requirements of the customers. If the same product is repeatedly offered, the investment climate is not improved. Therefore, there is always a demand for fresh financial product designs.
2. The business sector was obliged to consider new financial products as a result of the declining interest rates.
3. Additionally, investors prefer not to be burdened with lengthy instruments. As a result, instruments with different maturity dates and call and put options are chosen.
4. Financial institutions are no longer the primary source of financing as they once were. Capital markets are now preferred by businesses as a source of funding. Companies must provide appealing conditions even on debt instruments in order to effectively access the capital markets and borrow money.

5. Due to several capital market frauds, investors have stayed away from the equities market in recent years. To get these investors back, there has to be enticing financial instruments.

Instruments After the Reform Era

Numerous novel instruments have been introduced to the capital market throughout the post-reform era. The majority of them are debt instruments. These instruments have been effectively sold at the retail level in addition to having a sound construction and design.

a. Fixed-rate bonds:

These bonds' interest rates are not set; instead, they are based on a benchmark or anchor rate. It is a notion that was initially established to address the declining market or to act as a buffer during periods of declining interest rates in the economy. It aids the issuer in hedging the loss brought on by changes in interest rates. The State Bank of India was the first financial institution in India to provide bonds with fluctuating interest rates to ordinary investors. The term deposit rate at the bank acted as the anchor rate for the SBI variable rate bonds. The anchor rate may also be the rate on Treasury bills. Because the anchor rate reflects economic variables, the interest rate is connected to it. These days, floating rate bonds utilize the NSE Mibor as their anchor rate. The interest rate on this bond always carries a predetermined markup over and above the anchor rate in order to entice investors. For IDBI bond offerings, the anchor rate was the 364-day treasury bill rate, and the fixed markup was 2%. Bonds with a floating rate guarantee that neither the lender nor the borrower suffer as a result of changing interest rates. Borrower firms offer floating rate bonds with a ceiling or a floor. If the interest rate increases, the lender gains because he receives a greater interest rate. If the interest rate falls, the borrower benefits because he may raise money at a cheap cost. The cap is the most interest the issuer may pay, while the floor is the least amount of interest a subscriber can receive, giving both the issuer and the subscriber a benefit.

The majority of the outstanding loans on the government market are simple fixed rate bonds. In order to meet the asset-liability management and risk-weighting requirements of the large investors, such as banks, the government issued two floating rate bonds in November and December 2001, with maturities of 5 and 8 years and a total face value of Rs 5,000 crore. FRBs benefit from the term premium while lowering the refinancing risk, making them diverse tools in debt management. FRBs are susceptible to interest rate risk, nevertheless. FRB is a cutting-edge tool in a low-interest rate environment, but it needs a thriving secondary debt market.

b. Bonds with no interest:

Zero interest bonds are offered at a significant discount to face value and do not bear any recurring interest payments. These bonds help both the issuers and the investors by lowering the risk associated with reinvestment for the investor and decreasing financing costs when interest rates are erratic for the issuer. When zero coupon bonds mature, they may be converted into equity with no cash outflow for the issuer or, after a certain amount of time, into conventional interest-bearing bonds. These bonds were first introduced to the Indian market by firms like Mahindra & Mahindra and HB Leasing and Finance. For individuals and institutional investors seeking secure returns who are prepared to keep bonds to maturity, these bonds are the best choice. In addition, there is no interest paid on these bonds, which would normally be taxed.Since there is no immediate interest obligation and the bonds may be converted into equity shares or non-convertible debentures at maturity, depending on the capital structure needs of the firm, these bonds are appealing to issuer companies with

projects that have a lengthy gestation time. A thriving secondary debt market is necessary for zero interest bonds to draw in investors.

c. Bonds at a Deep Discount:

A deep discount bond is a zero-coupon bond that is sold at a discount to face value and has a very long maturity, such as 15 years or more. The first financial institution to provide DDBs was the Industrial Development Bank of India in 1992. By enticing the investor to become a "lakhpati" in 25 years, the issuers have effectively promoted these bonds. Additionally, these instruments have imbedded "call" and "put" options, giving the issuer and the investor the ability to redeem their investments early at a set price and date. The issuer no longer has to worry about sporadic cash flow issues, and the money may be used for infrastructure projects with lengthy gestation periods. DDBs and zero interest bonds have been produced in a wide variety. These are a few of them. :-

Zero Interest Secured Premium Convertible Bond:

At the conclusion of a year, the investor may convert his bond into equity shares at a 30% discount from the average price. A comparable option of conversion into two equity shares is offered at bond maturity. If the conversion price is less than the face value, the issuer will redeem the difference.

A warrant might also be affixed to the bail. Fully Convertible Zero Interest Debenture: These debentures do not pay interest to the investors. Fully paid, fully convertible debentures will, however, automatically and compulsorily convert into shares after a certain length of time. If a corporation decides to do a right offering before allocating equity, the effect would be the conversion of stock shares into FCDs. Holders of FCDs will be presented with securities, as the firm may decide.

d. Debentures Rated for Auction

It is a secured, redeemable, non-convertible product with market-based interest that is offered privately. ARDs are a cross between commercial papers and debt obligations. This brand-new instrument was created for Ashok Leyland Finance by ANZ Grindlays. This was a three-year instrument with a zero-coupon rate that was offered for sale at a reduced price. After three months had passed since the first issuance, the business bought back the ARDs and reissued them via new auctions.

At quarterly auctions, the interest rates were negotiated; this process lasted for three years. Through this special zero-coupon instrument, ALF was able to obtain Rs 30 crore. Although technically a short-term instrument, ARD offers the firm long-term financing.

e. Insured Paper

In developed markets like the US and the UK, it is a well-liked method of fund-raising. The pooling of home mortgages in the US in the 1960s marked the beginning of asset securitization. This idea now encompasses a. a broad variety of financial assets owned by companies and financial institutions, including receivables and mortgages. A corporation may raise money via securitization by selling off its receivables. These receivables are turned into securities and sold to investors with plenty of cash. The yield is represented by the receivables that were sold to investors at a discount. Illiquid assets are bundled and turned into marketable securities known as pass-through certificates via the process of securitization. Asset-backed securities are the name given to these securities. Mortgage-backed securities are the name given to the final product if the asset being securitized is a home loan. They are

known as collateralized bond obligations in the case of bond receivables and as collateralized loan obligations in the case of industrial loan receivables.In a securitization deal, the originator transfers prospective receivables to a special purpose entity, which then issues pass through certificates to investors as securitized assets. Pass through certificates are financial products that prorate the cash flows from the underlying loans.

Four kinds of asset-backed securities exist:

Mortgage investment route for real estate. When principal and interest payments are passed through to investors on a schedule comparable to the assets, the security is referred to as a pass-through security. The balance sheet of the issuer no longer includes these assets. A debt obligation with an asset-backed bond has a different interest and principal payment schedule than the asset itself. The Assets still appear on the balance sheet of the Issuer. In contrast to asset-backed bonds, pay-through assets do not stay on the issuer's balance sheet. The principal and interest payments are transferred to one or more regular classes of securities and one residual class when using a real estate mortgage investment instrument. The REMIC receives assets via a non-taxable transfer. PTCs are issued and increasingly common in India.

After that, the Securities may be listed on the NSE. The securities were traded in the secondary market since they were listed and negotiable instruments. Asset securitization refers to the procedure since the securities are assets for the seller. The procedure is known as "debt" securitization because once it is listed on a stock market, it turns into a debt product for the investor. Securitization is primarily driven by the need to raise low-cost capital from fresh sources in an off-balance sheet fashion. Once an asset is securitized, it is removed from the issuer's balance sheet. It increases the investor's return and the value of his investment portfolio. Compared to factoring or bill discounting, securitization is far better. Securitization is a medium- to long-term source, while bill discounting is a short-term one. In comparison to securitization, bills discounting involves more paperwork. As the factor buys a company's receivables at a discount, factoring is quite similar to securitization. However, factoring does not include rating or the development of a secondary market. Additionally, factoring has developed as a tool for trade finance as opposed to medium- or long-term financing.

f. Debt obligations with Collateral:

Collateralized debt obligations are created by securitizing corporate commitments such asset-backed securities, note bonds, and corporate loans. Collateralized bond obligations make up a CDO collectively. Credit linked notes and collateralized loan obligations are members of the same financial family. This tool is used by banks and other financial organizations to fulfill legal requirements and boost income. The Basel Committee on Banking and Supervision created the Basel Accord in 1988, which mandates that banks in the majority of industrialized nations hold risk-based capital equal to 8% of the outstanding balance of commercial loans. Due to the poor profits on commercial loans and the high risk-based capital needs, retaining them is not appealing. Banks may reduce the amount of debt on their balance sheets by securitizing their loan portfolios, as well as profit from these portfolios. A CDO's structure is made up of several layers, referred to as tranches, that are created by combining the underlying assets. A pool of assets made up of corporate loans and bonds with a comparable seniority and term will be available for each tranche. A credit rating agency then rates and markets these tranches.

Although there is a bigger default risk with these products, investors will get a higher yield. After the Enron scandal, off-balance sheet finance gained a bad reputation around the globe. Enron credit was a component of several CDOs' underlying exposure, and they defaulted. Along with American banks, European banks and the Bank of Japan are also using this tool

more often. Due to unfavorable market circumstances and a lack of regulatory rules, the ICICI Bank's maiden CDO offering failed to take off in March 2002 and was recalled. The average maturity of the issuance was decreased to around two years by the bank in February 2004. This changed the product structure. Institutional investors bought up the Rs 100 crore CDO offering. Through this offering, the ICICI bank offered corporate loans made to 15 borrowers of various sizes and in 11 different industries in order to generate new assets and improve exposure management in certain industries.

g. Bonds with inverse float:

The Indian capital market's newest arrival is this group of bonds. Bonds with an interest rate that fluctuates and is inversely correlated to short-term interest rates are known as inverse float bonds. The Mibor or another rate might be the floating rate. If the Mibor decreases, the investor's return increases, and vice versa. The variable rate is subtracted from a set benchmark rate to get the actual rate due on these bonds. If the six-month Mibor is at 6% and the fixed benchmark rate is at 12%, the interest on these bonds will be due at 6%.

With the help of these bonds, investors may profit from low interest rates while generating substantial profits. Due to the extreme volatility of interest rates, the investor must constantly monitor interest rate behavior during the whole bond duration or risk receiving a subpar return. Therefore, interest rate risk must be managed by both the investor and the issuer. The issuer gains if interest rates rise since his bonds' coupon yields will drop despite increased interest rates. In 1990, inverse float bonds were first offered on the US market. In August 2002, the Aditya Birla group, Grasim, and Hindalco issued in India inverse float bonds. The first non-banking finance business to raise money via the sale of inverse float bonds was The Cholamandalam Investment and Finance business Limited.

Indian Derivatives Market

Derivatives are important financial products in established financial markets in addition to capital market and money market tools of generating cash. These are the financial instruments, such as shares, commodities, or currencies, whose value is derived from the value of another item. Financial derivatives are seeing a very fast market expansion. In this section, we'll strive to comprehend how derivatives work and how significant they are to the Indian financial market.

Derivative is derived from the verb "to derive." It indicates that the value of the underlying asset from which the derivatives receive their value. To put it another way, "Derivative, or derivative securities, are contracts between two parties, whose value is derived from the value of underlying widely held and easily tradable assets, such as agricultural and other physical commodities or currencies, or short-term and long-term financial instruments, such as inflation rate, share prices, currency rates, and commodity prices. The two types of derivatives are commodity derivatives and equity derivatives.

Commodities include wheat, rice, cotton, gold, pepper, turmeric, maize, crude oil, and others. Financial derivatives: These are financial products in which the underlying asset is a financial product, such as a bond, stock, foreign currency, or Treasury. Future contracts are precise delivery forward contracts that are transferrable.

These are standardized contracts that commit parties to buying or selling a certain amount of a financial instrument or a commodity at predetermined prices in a future month. These agreements are highly standardized agreements between buyers and sellers' shorts and longs, respectively.

CONCLUSION

In conclusion, The PSU bond market is essential to India's debt market since it helps public sector organizations expand and finance their demands while also giving investors looking for steady returns investment alternatives. Policymakers, regulators, issuers, and investors must work together to address the issues and seize the potential in the PSU bond market. The PSU bond market may continue to develop as an important element of India's financial landscape by establishing a favorable regulatory environment, supporting market reforms, and adopting responsible risk management procedures. To successfully manage the distinct features and dynamics of the PSU bond market, investors and market players must remain educated and practice due diligence. Proper systems for credit assessment, credit rating processes, and risk management procedures must be reinforced to address concerns about credit risk. It may be necessary to take actions to promote more stable trading platforms, promote market-making, and increase market transparency in order to increase secondary market liquidity for PSU bonds.

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CHAPTER 17

EXPLORES THE SIGNIFICANCE AND FUNCTIONS OF FINANCIAL SERVICES AND REGULATIONS

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ABSTRACT:

Financial services and regulations are integral components of the global financial system, serving as critical enablers of economic growth, stability, and investor protection. This paper explores the significance and functions of financial services, including banking, insurance, investment, and asset management, in facilitating capital allocation and risk management. It also examines the role of financial regulations in safeguarding market integrity, ensuring consumer protection, and mitigating systemic risks. The study delves into the complexities and challenges of financial regulations in a rapidly evolving technological and globalized landscape. Understanding financial services and regulations is essential for policymakers, financial institutions, investors, and consumers, as it enables informed decision-making and contributes to the development of a robust and resilient financial ecosystem.

KEYWORDS:

Asset Management, Banking, Capital Markets, Credit Cards, Credit Unions, Cryptocurrency Regulations.

INTRODUCTION

Financial Services

Financial services are auxiliary or supporting services that assist in the borrowing and lending of credit in an indirect manner[1], [2]. Numerous financial operations, such as:

1. Making payments and financial settlements, are made easier by these services.
2. The purchase and sale of securities
3. Adding support to risk management
4. Assisting businesses in creating and developing cutting-edge means of money raising.

Financial services are, to put it briefly, vital and crucial components of the financial system. They support investing and saving, improve trading in securities, and aid in spreading risk to those who are willing to take it. Some of the financial services are explained in depth in the sentences that follow.

Insurance

A legal agreement between two parties known as an insurance contract requires the insurer to commit to paying a certain sum of money should a specific eventwhich might be definite or uncertainoccur[3], [4]. The other partytheinsuredpays a certain amountthepremiumin return. The terms assurer or underwriter and assured are used to refer to the insurer and the insured, respectively. The policy is the name given to the document that contains the contract. It is a crucial financial service that is offered to eliminate or reduce the danger of losing life or property. As it offers security and stability to the company against several risks including fire, accidents, mortality, and other unanticipated uncertainties, insurance is crucial to the economic development of a nation.It inspires businessmen to make risky choices in their respective sectors of business.It assists the government in carrying out its responsibility to

provide social assistance to the impacted families.Insurance firms use the premium money they receive from policyholders to finance infrastructure or industrial projects or to buy assets[5], [6].

Insurance Forms

The insurance service provides coverage for a variety of hazards. Here are a few of the significant ones:

1. Health insurance is a contract that covers the policyholder's medical, surgical, or hospital expenses in the event of illness. The value of health insurance has increased as government spending on healthcare has decreased [7], [8].
2. General insurance, also known as non-life insurance, offers short-term protection against risks such as fire, automobile accidents, maritime cargo, and other atypical categories including chickens, water pumps for agriculture, and huts [9], [10].
3. Micro-insurance is insurance for very low-income households that insures a little amount for a negligibly small premium. It is designed to provide protection against things like weather, accidental death, life, and health.

Historical Evolution of India's Insurance Industry

There were around 245 life insurance businesses in India prior to the nationalization of the insurance industry. All of these businesses were acquired by the Life Insurance Corporation of India in 1956, and the General Insurance Corporation seized control of general insurance in the nation in 1972. For a very long time, LIC had control over almost the entire life insurance sector. The biggest insurer in the whole globe is LIC.

According to the legislation, LIC is required to invest at least 50% of its capital in low-yielding government securities. Along with its four subsidiaries, National Insurance Company Limited, New India Assurance Company Limited, Oriental Fire and General Insurance Company Limited, and United India Insurance Company Limited, GIC, like LIC, regulated the general insurance industry. According to the Malhotra Committee's recommendations, financial sector reforms resulted in the liberalization of the insurance industry in 2000. As a result, businesses from the private sector were permitted to operate in the insurance industry. There are now 15 general insurance firms and 16 private life insurance companies operating in India's insurance sector. mutual funds

A mutual fund is described by SEBI asa fund established in the form of a trust to raise money through the sale of the units to the public or the public under one or more schemes for investing in securities, including money market instruments. Mutual Funds take money from the general population and invest it on their behalf.

For the average person who lacks the time, resources, or competence to directly engage in stocks, mutual funds provide a way to participate in the stock market. In summary, mutual funds are crucial to the financial system because they direct small investors' savings toward India's productive industries. Mutual funds can allow modest investors a chance to profit from financial growth while assuming little risk.

The benefits of mutual funds

1. **Professional management:** The average individual could lack knowledge on how to deal with the financial market. Mutual Funds are managed by qualified managers who have the necessary training, expertise, and legal authorization.

2. **Diversification:** Mutual Funds invest in a variety of businesses, reducing risk and increasing investment diversification.

3. **Convenience:** Mutual Funds lessen the amount of paperwork and administrative hassles associated with capital market investments.

The cost of administration tends to be lower because of the volume of the transaction.

4. **Transparency:** Transactions involving mutual funds are open, and investors get regular updates on the status of their investments.

5. **Tax advantages:** Investors in mutual funds get income tax advantages on the portion of their income that they save in mutual funds.

Mutual Fund Types

Classification of functions:

Open-ended plans: These plans do not have mutual funds with specified goal amounts, corpuses, or redemption periods.

An example of an open-ended mutual fund is the UTI unit scheme. Closed-ended schemes: Under these plans, mutual funds have a defined corpus and a redemption term that typically lasts between two and five years.

The maximum number of days the plan is active is 45. Interval scheme: Mutual Funds that participate in these schemes share the characteristics of the two schemes listed above.

Categorization of a Portfolio

Income funds: These funds provide investors a consistent stream of income. Here, funds are invested in assets that provide a fixed income, such as bonds, debentures, government securities, etc. Both the risks and the profits are modest.

Growth-oriented funds: large risk, large rewards for investors are characteristics of these products. Balanced funds:

These investments provide both regular income and capital growth. cash market Mutual funds have tremendous liquidity but provide modest returns. Investments are made in short-term money market products like certificates of deposits and treasury bills.

Geographic Description

Domestic funds - These are the plans to mobilize householders' savings. These funds are used to raise money, which is then invested in domestic equities. On the other hand, offshore money is international in character.

These funds are used to raise money, which is then invested in international securities.In addition to the funds indicated above, there are other ones. Sectoral funds for investments in vital industries like infrastructure and energy are among them. a unique fund, such as the 1986 Children's Gift Growth Fund and theme-based funds

Growth and Performance of the Indian Mutual Fund Sector:

Since the 1990s, the mutual fund sector in India has expanded quickly. As of June 30th, 2005, there were around 30 mutual funds and 1.65 lakh crores. This has increased competition and led to the development of new items.

DISCUSSION

Merchant Banking

There are residuary non-banking firms that mobilize public savings in addition to banks and non-bank financial intermediaries. They receive public deposits and often mobilize deposits from a large number of modest depositors. One of these residuary non-bank financial institutions is the merchant bank. Merchant banks are sometimes referred to as "accepting and issuing houses" in the UK and "investment banks" in the US. Instead of capital, they focus more on offering financial services. As a result, these banks don't need a lot of capital. Comparatively speaking, merchant banks act more as "brokers," "intermediaries," or "arrangers" than do commercial banks, which primarily deal with taking deposits and making loans. The following are the main characteristics of merchant banking:

1. They provide financial services and advice for a charge.
2. They focus more on wholesale banking; hence, they are connected to industrial firms.
3. Their major focus is on brand-new securities.
4. They are primarily responsible for selling and guarantying corporate securities.
5. They provide all services linked to the issuance of securities, including underwriting, application acceptance, securities allocation, money collecting, delivering share certificates, etc.

Indian merchant banking

Commercial banks like SBI, Canara Bank, and Bank of Baroda provide these services via their subsidiaries, SBICAP (SBI Capital Markets Ltd.), CANFINA (Canara Bank Financial Services Ltd.), and BOB Fiscal (Bank of Baroda Fiscal Services). Other private consultancy firms like DSP Financial Consultants, Credit Capital Finance Corporation Ltd., J.M. Financial and Investment Services Ltd., etc. deal with merchant banking services for Indian as well as foreign companies. Developmental banks like ICICI, IFCI, and IDBI also offer these services. The number of merchant banks and their operations have increased in tandem with the stock market's expansion. For its development and regulation, SEBI has offered a variety of rules. Many commercial bankers lack knowledge of international financial standards. The Indian financial system's growing globalization has made a deeper knowledge and more activity necessary to capitalize on the current developments. To handle the task on a global scale, Indian merchant bankers must get training.

Venture Capital

It is a novel financial service that first appeared in India in 1987 and the US in the 1970s. It has to do with taking big risks, as the name suggests. The fresh, unproven, and unregistered businesses that lack access to traditional sources of funding are often given venture capital. Venture capital businesses provide managerial and marketing services to the fledgling company enterprises in addition to just financial support. The demands of technology-focused and knowledge-intensive commercial enterprises in the sectors of electronics, chemicals, plastics, biotechnology, etc. are met through venture finance. The venture capital companies are willing to take on significant risk in the hopes of receiving significant rewards.In a nutshell, a venture financing company offers the following services: seed money, or the first cash for beginning a business; extra capital for developing a business; equity financing for takeover; funding for globalizing a business; and capital for business diversification.

Venture capital funding in India has gotten off to a slow start. Although it has grown quickly in a short period of time, there is still a lot of room for growth in the expanding Indian

economy. Commercial banks hold and are the primary founders of the majority of significant venture capital firms. These include RCTFC Risk Capital and Technology Finance Corporation Ltd., the UTI Technology Development and Information Company, and the IDBI Venture Capital Fund.

Credit Score

The Indian financial system has grown as a result of financial sector reforms, and a rising number of both new and veteran financial actors are joining it. New financial products are being released, and the structure of the financial industry has become very complex. The complexity of the market is hard for the average investor to comprehend. The tendency toward privatization has increased the risk associated with credit-related activities at the same time. An evaluation of the borrower's creditworthiness is called a credit rating. A public judgment on a borrower is known as a credit rating. It is believed that an investor would base his investment choices on the debt instrument's credit rating. The financial performance of individuals, organizations, financial goods, and governments is assessed by credit rating agencies in FM.

Value of a Credit Rating

Credit rating agencies are a crucial component of a nation's financial system. By giving investors a ready-made assessment of the debt instrument, credit rating saves them time and effort. As a marking tool for investments, credit rating is also helpful for those looking to raise capital. With less advertising, a company with a solid credit rating will find it simpler to borrow financing. In the financial sector, credit ratings encourage effectiveness, stability, and openness. Even the financial market regulators gain from the credit rating process.

Indian credit ratings

The following criteria are used to rate a financial instrument of a company:

1. Business evaluation
2. Analyzing finances
3. Management assessment
4. Fundamental investigation

Business analysis includes the evaluation of a company based on the industry risk examined by the demand and supply position, competition type, industry-related government policies, company market positions, market share, competitive advantages, distributional aspects, strengths and weaknesses, location-related aspects of the company's cost structure, technological advantages, and company's legal position.An evaluation of the company based on its accounting practices,anticipatedprofits,cash flows, andfinancial flexibility is included in financial analysis.

By evaluating a company's capacity for planning and managing, overcoming challenging circumstances, setting objectives, and developing plans. Fundamental analysis includes a review of the company's capital sufficiency or liquidity management, credit monitoring system, profitability, and non-profit income streams, as well as interest rate sensitivity.

Companies who want to be graded must fill out forms with the necessary data within the aforementioned headings. To confirm the provided information, a team of experts from a credit rating organization may visit with representatives of the business. Finally, the report with a rating and suggestions is submitted by the Credit Rating Committee. Ratings may be raised, lowered, or left unchanged.

The SEBI in India has published a number of rules for the credit rating agencies. In recent years, the credit rating industry has seen remarkable growth. Although there are established standards for assessing and evaluating the performances of financial assets, there is some subjectivity in the process. It's possible to doubt the credit rating companies' own qualifications. There are few instances when a financial institution received the highest rating from these organizations yet nonetheless collapsed. The credit rating companies don't conduct any audits. They are entirely dependent on the details provided by the corporation in the inquiry. These and other restrictions on the credit rating process need to be addressed.

Forfeiture and Factoring

Due to recent economic changes and the altered business climate, new financial services such as factoring and forfeiting have evolved. Mergers and acquisitions have become a highly typical occurrence as a result of heightened rivalry and a desire for greater market share. A corporate establishment must arm itself with a defense against these unfavorable worldwide tendencies. Possessing the ability to convert outstanding credit into cash liquidity is one necessity for sustaining competitive positions in the market. The financial services that might help commercial enterprises in this regard are factoring and forfeiting.

Factoring:

This ongoing agreement between a financial intermediary and a commercial enterprise allows the factor to buy the client's accounts that will eventually be paid by customers. The following is how the factoring process operates:

1. A customer orders electrical equipment from Company A.
2. The client receives the equipment along with an invoice or bill for, say, Rs. 30,000 that must be paid within, say, 90 days.
3. The customer gives the factor, such as Can bank Factors Ltd., a copy of the invoice.
4. The factor may pay up to 80% of the invoice's total amount. It implies that the consumer receives Rs. 24,000 in cash right now.
5. The factor is responsible for providing the client with periodic statements of accounts and doing any necessary follow-up measures with the customer.
6. The customer pays the factor.
7. After receiving the customer's payment, the remaining 20% is given.

All three parties engaged in the process the client, the consumer, and the factor benefit from factoring. As soon as they supply products or services to the customer, the customers get instant cash from the factor. Since the factor bank handles the client follow-up on their behalf, they don't need to worry about it. The customer or corporate entity may then focus on the operations related to manufacturing and marketing. The consumer is given enough time to make payments and is not required to submit any paperwork or participate in any administrative processes. The customers' total liquidity improves, and the factor receives service fees.

Forfeiting is a financial service in which a forfeiter pushes 100% financing to the exporter against a letter of credit, bill of exchange, or both. Like factoring, forfeiting operates in a similar way. Here, an exporter gives the forfeiting agency the trade receivables in exchange for 100% cash payment to the exporter. Therefore, it is the forfeiting company's obligation to recover payments from the importer. A forfeiture provides an exporter with 100% cash and releases him from all hazards associated with foreign commerce. In 1992, the RBI recognized forfeiting as a method of export financing, and since then, this area has seen some advancement. Two participants in the Indian financial industry, EXIM Bank and Global Trade

Finance Limited, provide forfeiting services to Indian exporters. The notion of financial services, its significance to the financial system, and the numerous forms of financial services emerging in India have all been covered in this subject. The requirements of economic actors for credit will rise as company complexity rises. However, at the same time, there will be a greater need for supporting financial services. From that perspective, learning about crucial components of such services can improve our comprehension of the Indian financial system.

CONCLUSION

In conclusion, Regulations and financial services are essential components of the contemporary financial system. Effective rules that support market integrity and investor protection must work in harmony with strong financial services that cater to the various demands of consumers and companies.

This is the foundation of a healthy financial ecosystem. To negotiate the financial landscape's complexity and adopt novel solutions while exercising caution and resilience, policymakers, financial institutions, and consumers must collaborate. dStakeholders may support long-term economic development, financial stability, and societal well-being by promoting a vibrant, inclusive, and well-regulated financial system.

To meet new and developing dangers to the financial system, financial rules must be flexible and forward-looking. Effective financial rules must include consumer education and financial literacy to provide people the capacity to make wise financial choices and safeguard them against predatory behavior.

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CHAPTER 18

A STUDY ONSECURITY AND EXCHANGE BOARD OF INDIA

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ABSTRACT:

The Securities and Exchange Board of India (SEBI) is the primary regulatory authority responsible for overseeing and regulating the securities market in India. This paper explores the significance and role of SEBI in fostering investor protection, market integrity, and the development of the Indian capital market. It delves into the functions and powers of SEBI, including its responsibilities in formulating regulations, enforcing compliance, and conducting investigations. The study also examines SEBI's efforts in promoting transparency, market efficiency, and financial literacy. Understanding SEBI is essential for investors, issuers, market intermediaries, and policymakers, as it enables informed decision-making, compliance with regulations, and contributes to a robust and transparent securities market ecosystem.

KEYWORDS:

Capital Market, Collective Investment, Depository System, Insider Trading, Initial Public Offering (IPO), Investor Protection.

INTRODUCTION

In the 1990s, India's capital market saw tremendous development because to changes in the financial sector. Small investors started participating in the stock market as well. The Indian financial system joined the international one. In light of these conditions, it was imperative to assure that:

i) The liberalization tendencies would continue.
ii) financial intermediaries are subject to certain rules to stop unfair business activities. In this lesson, we'll talk about several crucial rules that the Indian financial system adopted in order to increase the capital market's flexibility and efficiency [1], [2].

Indian Reserve Bank

The RBI, as the nation's central bank, serves as the top supervisor of the Indian financial and monetary system. A Central Board of Directors, four Local Boards of Directors, and a committee of the Central Board of Directors oversee the management of the RBI. The majority of the 22 regional offices of the RBI are located in state capitals[3], [4].

Note Issuing Authority: The RBI is solely responsible for printing all coins and notes other than those worth one rupee. 18 regional issue offices are responsible for carrying out this duty. Four note presses produced the notes.

1) The Currency Note Press in Nasik
2) The Bank Note Press in Dewas
3) Mysore Press
4) Salboni Press

The Bank has the authority to issue notes backed by government, international, or gold coin assets.

B) Monetary Authority of the Country:

The RBI, as an apex organization, formulates the monetary policy for the nation[5], [6]. The RBI controls the cost and accessibility of credit in the nation via measures including the Bank Rate, Open Market Operations, and Cash Reserve Ratio. Financial sector changes have mostly been implemented via the use of monetary policy. The RBI also makes an effort to control the use of credit in order to promote the flow of bank credit into small businesses, agriculture, housing, and other sectors[7], [8].

C) Government's Banker:

The RBI oversees the financial operations of the Central and State governments in its capacity as the government's banker. In light of this, the RBI:

i) Oversees public debt
ii) Offers financial services to the government
iii) Manages the banking accounts for the government kept at Central Accounts in Nagpur
iv) Manages specific government funds and
v) Loans to the government.

D) Financial system regulator:

The RBI is appointed as a financial system regulator in order to safeguard depositor interests and provide simple banking services to the general public. Under this role, the RBI:

(i) Monitors the operations of commercial banks, non-bank financial institutions, and cooperative banks; and
(ii) Takes significant steps to enhance and reform the financial system's structure.
(iii) Oversees and controls activities relating to foreign exchange
(iv) Develops the money and capital markets.
(v) Assumes responsibility for compiling and disseminating data pertaining to money, banking, and the economy [9], [10].

E) Promotional Role of the RBI:

The RBI has several other responsibilities outside the typical ones of a central bank. The RBI must carry out certain proportionate and developmental tasks since it is the central bank of a growing nation like India.

The RBI has encouraged the creation of many specialized financial organizations under this, including NABARD, Finance Limited, etc. In a same vein, the RBI, ICICI, IDBI, National Housing Bank, Infrastructure, and Development have made conscious efforts to promote credit flow to the economy's core sectors.

The RBI develops rural credit and microcredit programs. In conclusion, the scope and importance of RBI's duties have evolved throughout time. With the financial sector becoming increasingly liberalized, maintaining financial stability has become a more crucial goal.

The country's financial industry has been strengthened and stabilized thanks to the RBI. To increase the flexibility and effectiveness of the Indian financial system, further measures are being adopted.

DISCUSSION

Organisation of SEBI

Although SEBI was founded on April 12, 1988, it wasn't until 1992 that it started to operate. The SEBI board of directors is made up of a chairman, two RBI officials, and two additional experts with knowledge of the securities industry. SEBI's primary goals are:

1) Investor Protection
2) Consistent Savings
3) Fair Business Practices by Issuers.
4) Support for effective financial services
5) Transparency.

Roles of the SEBI:

The work the SEBI does may be divided into two categories:

Regulation and developmental functions and the SEBI's regulatory responsibilities include:

(i) registering and regulating the activities of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisors, and other intermediaries connected to the securities market.
(ii) Register and oversee the operations of depositories, depository participants, custodians of securities, foreign institutional investors, credit rating agencies, and any other securities market intermediary that the SEBI may define by notice.
(iii) Register venture capital funds, collective investment schemes, and mutual funds, and supervise their operation. Only after getting a certificate of registration from the SEBI are any of these intermediaries able to do business in the securities market. Any intermediary's registration may be revoked by the SEBI if it is shown to be engaging in unfair business activities in the capital market.
(iv) Regularly inspects stock exchanges to provide a free and fair environment for investors.
(v) Develops rules to ensure the security market in India is secure, honest, and stable.

The SEBI engages in the following activities under its development functions:

i) Promoting investor education and awareness of the securities market.
ii) Supporting the securities market's self-regulation mechanisms.
iii) Giving market intermediaries training.
iv) Promoting a code of conduct and ethical behavior.
v) Gathering information on stock market activity and publicizing it.

Performance of SEBI's Key Areas

The SEBI has been effective in bringing about improvements in the capital market since its founding. The SEBI, a totally independent organization, has been a powerful force in regulating and advancing the securities industry. Each year, a comprehensive examination must be performed on at least 20% of the active brokers. To make sure that they are kept in the proper format, SEBI has been inspecting the books and records of subsidiaries. The SEBI took on 1,073 cases for inquiry between 1992–1993 and 2005–2006, of which 836 have been resolved. These incidents involve insider trading, overruling takeover laws, and market rule manipulation. All mutual funds are registered with SEBI in accordance with SEBI Regulation, 1993. Several mutual funds were subjected to disciplinary action in 2001-0 for

breaking the regulations. The SEBI encourages self-regulatory organizations to share the burden of policing capital market activity. They must abide by the same regulations for registration, inspection, and SEBI enforcement. However, they can more effectively stop deceptive practices in the financial market since they are better aware of the reality on the ground. The main goal of SEBI has been to protect investors' interests. Numerous rules are issued to them by it. It has implemented an automated method for managing complaints, which facilitates quicker settlement of issues. The "Guidance Division" of SEBI is responsible for handling complaints. The redressal percentage, according to the claim, is 94.53%.

Regulatory and Development Authority for Insurance

After the insurance industry was privatized, there was a need to control its future expansion. The IRDA was established by the IRDA Act of 1999 with the purpose of growing and overseeing the nation's insurance industry. Initially known as the Insurance Regulatory Authority, it gradually added a promotional and developmental component to its regulatory job while still maintaining its status as a body offering recommendations and explanations. As a result, it was given the name IRDA. The IRDA has a chairman, four full-time members, and four part-time members.

The IRDA's responsibilities are outlined in Section 14 of the IRDA Act, 1999, which is as follows.

1. To control, encourage, and assure the expansion of the insurance industry.
2. To provide the applicant with a certificate of registration and, if necessary, to renew or revoke it.
3. To safeguard the policyholders' interests in the settlement of claims and the terms and conditions of the policy.
4. Defining the standards of behavior, educational requirements, and hands-on training for insurance businesses and agents.
5. To manage and regulate general insurance-related prices and terms and conditions.
6. To make inquiries, carry out inspections, and carry out investigations, including audits of an insurer, intermediaries, and other connected parties.
7. Specifying the way in which the insurer and intermediaries would preserve and submit the books of account
8. To control how insurance companies spend their money.
9. To control the solvency margins.
10. To resolve conflicts that may develop between an intermediary and an insurer.

Role and effectiveness of IRDA

Since its establishment, the IRDA has made several changes to try to advance and regulate the insurance industry. For the purpose of keeping track of every new financial product that an insurance company introduces, IR has established a file and use method. Each business is required to provide all relevant information, together with copies of the terms and conditions, to the IRDA. Second, the IRDA has outlined the necessary academic credentials for insurance brokers. Thirdly, the IRDA and Indian Institute of Management have signed a Memorandum of Understanding to enhance research and development in the insurance business. Fourthly, the IRDA has taken a number of actions to safeguard policyholder interests. The policy papers have to be published in plain and understandable language. Last but not least, the IRDA has made it mandatory for every insurer to do business in rural regions in order to expand insurance service there. The IRDA has been playing a significant role in the Indian

economy as well as the global one thanks to the risk insurance it offers to shippers, importers, and the financial institutions that provide credit for operations connected to international commerce. Through its activities in several other nations, the IRDA supports the government's development of the export industry. The necessity for a regulatory body that would oversee and advance insurance-related topics arose as a result of the insurance sector's privatization. The IRDA is well equipped to handle the problems at hand. Regulation of these activities is urgently needed given the complexity of the financial system and its development. It is a very challenging undertaking to liberalize the financial industry while yet maintaining transactions in this sector to reduce losses to shareholders.

Monetary System

In the years after independence, the economic landscape underwent a profound transformation, which led to the economy's tremendous growth in a wide range of industries. Both a quantitative increase and a diversity of economic activity have occurred. The lessons learned during the 1980s have led to the conclusion that India requires effective financial systems in order to reap the rewards of a growing dependence on voluntary, market-based decision-making.The financial system may be the most significant institutional and functional tool for transforming the economy. Finance serves as a link between the present and the future, and whether it's through the allocation of savings for investments or their efficient, effective, and well-informed use, the effectiveness with which the financial system carries out its duties determines how quickly broader national goals can be achieved. The phrase "financial system" refers to a collection of interconnected tasks or services that come together to fulfill a certain objective. It consists of many marketplaces, institutions, tools, services, and procedures that have an impact on the production of savings, investment capital, and growth.Van Horne described the financial system as the process by which financial markets distribute savings effectively to final consumers or investors in real assets in an economy. The goal of the financial system, in Christy's opinion, is to "supply funds to various sectors and activities of the economy in ways that promote the fullest possible utilization of resources without the destabilizing consequence of price level changes or unnecessary interference with individual desires."The system's principal purpose, according to Robinson, is "to provide a link between savings and investment for the creation of new wealth and to permit portfolio adjustment in the composition of the existing wealth." According to the aforementioned definitions, the financial system's main duties include mobilizing savings, distributing them for industrial investment, and encouraging capital creation to quicken the pace of economic expansion.

The Financial System's Concept

Financial institutions, markets, tools, and services are all involved in the process of saving, financing, and investing. Above all, regulation, control, and monitoring are equally important. Financial management is thus a crucial component of the financial system. According to Goldsmith, there is "...a case for the hypothesis that the separation of the functions of savings and investment, which is made possible by the introduction of financial instruments, as well as the expansion of the range of financial assets, which results from the establishment of financial institutions, increase the efficiency of investments and raise the ratio of capital formation to national production and financial activities, and through the use of financial institutions,

Financial System Interrelationships

In a contemporary economy, a financial system offers services that are crucial. The cost of transactions is decreased by using a commonly used medium of exchange. Trade is

facilitated, which promotes manufacturing specialization. Financial assets with alluring yield, liquidity, and risk attributes stimulate monetary saving. Financial intermediaries improve resource use efficiency by assessing alternative investments and keeping an eye on the actions of borrowers. An economic agent may pool, price, and trade risks in the markets with access to a range of financial instruments. A thriving economy is built on trade, the effective use of resources, saving, and taking calculated risks. In truth, the nation might do this with the financial system's active assistance. One of the primary inputs to development, the financial sector has been regarded as the catalyst for the economy's fastest growth.

The structure of India's financial system

The Indian financial system may be divided into two major categories:

The organized and unorganized sectors

The financial system is further segmented into service providers and customers. Financial institutions provide their products and services to individuals, companies, and the government. They are the financial services' customers. The lines separating these areas are not always distinct. Despite the fact that financial systems vary from nation to nation, there are numerous commonalities across financial service providers.

Organized Financial system in India

The organized financial system is made up of a sizable network of banks, other financial institutions, and investment firms, as well as a variety of financial instruments, all of which operate in reasonably established capital and money markets. The commercial and cooperative banking structures are primarily responsible for providing short-term financing. Twenty-eight top public sector banks are in charge of nine tenths of this banking industry. A network of cooperative banks and land development banks exists at the state, district, and block levels in addition to commercial banks. Banks have a significant role in the financial system, accounting for around two thirds of all assets. Recently, Indian banks have expanded their services to include factoring, leasing, mutual funds, and commercial banking.

The following subsystems make up the organized financial system:

System of banking

1. System of cooperatives
2. A system of development banking
3. Financial markets
4. Financial institutions and corporations.

The structure of financial institutions in India has grown and diversified throughout time. The system has evolved in three domains: cooperative, private, and state. Both the cooperative sector and national corporate entities do a good job of serving rural and urban communities. More than 4,58,782 entities are involved in distributing credit to the different sectors of the economy.

Unorganized Financial System

The unorganized financial system, on the other hand, consists of generally unregulated moneylenders, local bankers, pawn brokers who lend money, landlords, dealers, etc. The Reserve Bank of India cannot directly manage this aspect of the financial system. Numerous other financial institutions, including as investment firms, chit funds, and others, are not

routinely controlled by the RBI or the government. But they are also subject to laws and regulations, making them part of the purview of the monetary authorities.

CONCLUSION

In conclusion, In India, the Securities and Exchange Board of India (SEBI) has established itself as a strong and effective regulatory body that supports the protection of investors, market integrity, and market growth. A well-regulated and thriving capital market ecosystem has been made possible by its proactive attitude, open regulations, and emphasis on investor education. Future investor confidence, market growth, and the long-term development of India's securities market will all depend on SEBI's capacity to adjust to changing market patterns and new problems. To promote a stable and sustainable securities market environment, investors, issuers, and market intermediaries must abide by SEBI's rules and directives. In order to sustain a fair, open, and effective securities market that contributes to the nation's overall economic development and prosperity, policymakers must continue to support SEBI's efforts. To handle new issues, preserve the effectiveness and resilience of the securities market, and resolve other regulatory authorities' concerns, ongoing cooperation between SEBI, market players, and other regulatory agencies is essential.

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CHAPTER 19

EXPLORES THE SIGNIFICANCE AND EVOLUTION OF INDIGENOUS BANKING IN INDIA

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ABSTRACT:

Indigenous banking in India has a rich history that dates back centuries, characterized by traditional and localized banking practices that predate the formal banking system. This paper explores the significance and evolution of indigenous banking in India, tracing its roots to ancient times and examining its role in supporting local economies and communities. It delves into the unique features and functions of indigenous banking, including informal credit systems, community-based financial institutions, and moneylenders. The study also analyzes the challenges and opportunities faced by indigenous banking in the context of modern financial systems and regulatory frameworks. Understanding indigenous banking in India is essential for policymakers, researchers, and financial institutions, as it provides insights into alternative financial models and opportunities for promoting financial inclusion and sustainable development.

KEYWORDS:

Cooperative Banks, Indigenous Banking, Moneylenders, Non-Banking, Rulers' Banks.

INTRODUCTION

India has a native financial system with a long history when it gained independence. The hundi, a still-in-use financial instrument akin to Western Europe's commercial bill, was created by this system. Both local commerce and trade between port cities and interior industry areas were financed by hundi. Banks often rejected them, particularly if they were supported by local bankers[1], [2].

Like the goldsmiths, merchants, and shippers of Europe's seventeenth and nineteenth centuries, native bankers mixed banking with other endeavors. They typically belonged to certain castes or groups, such as the Multanis, Marwaris, and Chettiars, and they varied in how much of their lending was financed by their own resources as opposed to deposits and other sources of money.

Indigenous bankers often approved the hundis that merchants issued, and sometimes they even offered personal guarantees for loans from commercial banks[3], [4]. The name "Shroffs," which likely initially referred to money changers but through time evolved to refer to the more sophisticated and powerful indigenous bankers, was used to refer to these bankers collectively.

The Sowkars and the Pathans were the principal moneylenders.

Indigenous banking was founded on a complex and wide-ranging network of personal connections that helped overcome the challenges of serving a large client base. Brokers weren't utilized to provide personal guarantees; instead, they were employed to make introductions and attest to the creditworthiness of certain borrowers. While some brokers brought together merchants and indigenous bankers, other brokers specialized in connecting indigenous bankers with commercial banks.

System of rural finance

Since the first Primary Agricultural Credit Society was established in 1904, the rural financial system has developed throughout time by adopting and putting into practice significant suggestions made by expert committees that have been periodically formed by the Government of India/RBI.

The Government of India and the RBI developed several new concepts, innovations, and novel approaches during the pre-reform period, and the Rural Financial Institutions responded very favorably by putting them into practice after the advent of the scientific and technological revolution in the sphere of agriculture[5], [6].

The Financial Sector

Two fundamental elements economics and law determine how the baking system is organized. The expansion of financial services is required by the economy's growth and the proliferation of banking habits[7], [8]. The structure and operation of the banks are impacted by the demand for various financial services.

Government rules are the outcome of national goals and ambitions, and they significantly affect the banking industry.

There are essentially two sorts of these restrictions. The first is rules that cause the creation of new banks to cater to the particular requirements of a variety of economic activity. Second, legislation that modifies the structure via liquidations, mergers, or nationalization.

RBI

The leader of this group is the Reserve Bank of India, which serves as the nation's central bank. The scheduled and non-scheduled commercial banks themselves may be classified into two categories.

Sector of Cooperatives

The village moneylender, who until recently was the main source of rural financing, has been replaced in the nation by the cooperative banking sector since the conditions under which he provided credit were often onerous and harmful to the growth of Indian agriculture[9], [10].

The industry is supervised by state law even if the Reserve Bank provides concessional financing to it.

The money market may be seen as existing somewhere in-between the organized and unorganized marketplaces.

Cooperative Credit Societies

The main cooperative credit organization is a grouping of local residents who are both borrowers and non-borrowers. The share capital of the society, member deposits, and loans from Central Co-operative banks are where the society gets its money from. Both the members' and the society's borrowing capacity is set. Members get loans to buy livestock, fodder, fertilizer, insecticides, tools, and other items.

Banks of Central Cooperation

These are a district's principal credit societies' federations. Within the parameters of the member societies' borrowing ability, these banks provide financing. They also manage every aspect of a joint-stock bank's operations.

Cooperative State Banks

A federation of Central cooperative banks, the State Cooperative Bank serves as a watchdog for the cooperative banking system in the State. It receives funding from the Reserve Bank of India via share capital, deposits, loans, and overdrafts. Instead of lending money directly to farmers, the State Cooperative Banks lend money to primary societies and central cooperative banks.

Banks for Land Development

The Land Development Banks, which are arranged into three levels, State, Central, and Primary level, meet the long-term credit needs of farmers for developmental purposes, such as the purchase of machinery such as pump sets, tractors, and other machines, the reclamation of land, fencing, drilling new wells, and repairing existing wells, etc. Farmers' mobile property is mortgaged by land development banks, cooperative organizations that provide loans.

DISCUSSION

Money Market

The availability and demand of investible funds are topics that the money market is interested in. In essence, it serves as a reserve for short-term money. A major portion of a country's financial transactions are cleared via the money market, which offers a mechanism for the lending and borrowing of short-term cash. It is a venue where borrowers, including organizations, people, and the government itself, make offers for short-term investible cash available to financial and other institutions.Money and financial assets that are near replacements for money are therefore covered by the money market. The money market is often anticipated to carry out the three major tasks listed below: To provide a mechanism for balancing the supply and demand of short-term cash. to act as a focal point for central bank intervention aimed at affecting the economy's overall level of interest rates and liquidity.

To provide consumers and producers of short-term funds enough access to meet their borrowing and investment needs at a price that effectively clears the market. The capital market is where financial institutions that provide medium- and long-term resources to borrowers meet the medium- and long-term financial demands of businesses and other activities. On the basis of the nature of their operations and the financing method they use, these institutions may also be divided into investment institutions and development banks. Financial institutions that provide their own shares and stocks to the public and provide long-term funding, particularly via direct investments in securities and the underwriting of capital issues of commercial organizations, are referred to as investing institutions. Investment banks, merchant banks, investment firms, mutual funds, and insurance companies are some of these entities. Development banks are financial organizations that provide businesses the resources they need to flourish, such as cash, initiative, and know-how, in order to promote industrial development.

Financial System Liberalization

In 1992–1993, a dramatic reorganization of the economic system was started, including industry deregulation, liberalization of foreign direct investment policies, public enterprise reforms, taxation system changes, trade liberalization, and banking sector reforms. Commercial banks, capital markets, and non-banking financing enterprises have all undergone financial sector changes.The goal of financial market reforms has been to strengthen the markets' foundation by addressing their fundamental flaws. The changes to the

money and foreign currency markets aim to widen and deepen them. Government securities market reforms aimed to improve the liquidity of government assets by creating a vibrant secondary market, issuing debt at rates near to market, and smoothing the maturity structure of debt. To preserve the integrity and safety of the market, reforms in the capital market have concentrated on enhancing disclosure requirements, building up the market infrastructure, and improving risk management programs at stock exchanges. The introduction of free pricing of financial assets like interest rates on government securities, pricing of capital issues, and exchange rates, the expansion of the number of players, and the introduction of new instruments are all aspects of structural changes in different market sectors.A component of banking reforms is enhancing the banks' financial stability and reputation. taken by the RBI, a commercial bank's supervisory and regulatory body operating under the Banking Companies Act

The 1949 Regulation Act. Capital adequacy standards in respect to the risks to which banks are exposed, prudential standards for income recognition, and provision of bad debts are all intended to strengthen the financial health of banks. The generally clear and healthy balance sheets of banks represent the elimination of external restrictions in rules of pre-emption of funds, benefits, prudential regulation, recapitalization, and write down of capital base. However, the reform movement has highlighted the fundamental flaws in banking systems that are dominated by the public sector. The Indian banking sector has to continue to strengthen its financial stability and adapt to the increased competition that a quickly liberalizing and globalizing economy would bring.

The Securities and Exchange Board of India was established in 1992 to encourage the growth and regulation of the securities market as well as to safeguard the rights of investors in securities. In order to enhance the quality of public offerings, share allocation, private placement, book building, acquisition of enterprises, and venture capital, SEBI has established recommendations for primary markets. secondary markets: introduction of screen-based online trading, dematerialization of shares through the establishment of depositories, trading in derivative securities, changes to the badla system to control volatility and transparency in transactions, insider trading laws to protect market integrity. The institutional and regulatory landscape in the domain of financial markets has drastically changed. The Reserve Bank of India has taken a number of steps with reference to NBFCs to promote disciplined NBFCs that operate under strong business standards.

The regulations aim to safeguard depositors' interests and offer better oversight, especially for institutions that take public deposits. The laws set a maximum amount that NBFCs may take in public deposits.

This cap is connected to credit score by a recognized rating agency. The heterogeneous nature, number, size, functions, and level of managerial competency of the NBFCs affect their effective regulation. An upper limit is also placed on the rate of interest on deposits to prevent NBFCs from providing incentives and mobilizing excessive deposits which they'" may not be able to service.

The financial system has become more market-oriented since the economy was liberalized in 1992–1993, when reform measures were also initiated. Market efficiency would be reflected in the widespread dissemination of information, the reduction of transaction costs, and the allocation of capital to the most productive users.

Further, freeing the financial system from government interference has been a key component of economic reforms.

Financial Intermediation and Savings

Saving

The term saving refers to the activity by which claims to resources, which might be put to current consumption, are set aside and so become available for other purposes. It represents the excess of income over current consumption. The total volume of savings in an economy, therefore, depends mainly upon the size of its material income and its average propensity to consume, which, in its turn, is determined by the level and distribution of the incomes, tastes and habits of the people, their expectations about the future, etc. As the size of the national income increases, the volume and ratio of savings may generally be expected to rise, unless the marginal propensity to consume is either equal to, or higher than the average propensity. This is very likely to be the case in countries where the standards of living are very low, and where the development policy places a heavy emphasis on the social objectives of raising the living standards of the poorer s of the community, or where the spending habits of the people are strongly influenced by the "demonstration effect)

Breakdown of Savings

Both public and private savings make to total savings. The government's usual budgetary channels and the retained profits of state firms together make up public savings.Home and business savings are also considered private savings.The home sector contributes the most to saves (77% in 1994–1995), followed by the public sector (6.8%) and the corporate sector (16.2%). In 1998–1999, savings in the form of tangible assets accounted for 36.1% of household savings.

Deciding Factors for Saving

The state's ability to perform its duties, the overall health of the economy, the tax system, the government's fiscal policy, as well as its pricing and investment strategies, all have a significant impact on the amount of public savings. Household and corporate deposits are also considered private savings. In democracies, they have by far the most significant position. In addition to economic factors the most significant of which are the level and distribution of income and the general fiscal, monetary, and economic policies of the state the size of household savings is determined by the capacity, ability, and willingness of the people to save. These traits are influenced by a variety of social, psychological, and political factors as well. Retained savings, depreciation, and other provisions made by businesses account for a significant share of all savings in industrialized nations. Because the savings of various types of commercial organizations are not only relatively modest but also difficult to separate from home savings, such funds are often associated with corporate savings. Corporate savings mostly rely on how profitable the businesses are, how they distribute dividends, make allowances for depreciation, etc., and how they retain current revenues for financial development plans. These, in turn, are significantly impacted by the overall status of the economy, the state's economic policies, and aspirations for the future).

Gross National Savings

On a gross basis, the savings include:

If you're talking about the private business sector, depreciation at book value. Savings in the form of financial assets in the case of the household sector without taking into account an increase in household liabilities, which are primarily made up of bank loans and advances, and in the case of physical assets, the difference in value of physical assets in terms of gross saving and net saving, which was as much as 43.2% in 1994–1995. This may be mostly due

to depreciation and changes in stock of unincorporated businesses, which account for 80% of family savings. In 1998–1999, the gross domestic savings rate was 23.4%.

Gold Household Sector

Gold has been kept out of the financial system for a very long time. Our savings projections do not account for it, therefore buying gold is considered spending. This actually goes against long-held tradition. The estimated $100 billion worth of gold hoards must be integrated into the mainstream of the financial system. Additionally, 90% of our $6 billion in yearly imports are used for investment-related jewelry purchases. According to the Committee on Capital Account Convertibility, gold should be considered as a "hybrid asset." According to the Committee, gold serves as a stand-in for foreign currencies and, due to its unique characteristics, is a cross between a financial asset and a commodity. The Committee on CAC recommended that "banks should be permitted to operate freely both in the domestic and international gold markets, sale of gold by banks and financial institutions should be freely allowed to all residents, banks should be permitted to offer gold denominated deposits and loans, and banks should be permitted to offer deposit schemes similar to gold accumulation plans.

Savings of the Household Sector in Financial Assets The financial assets in 1998-99 were bank deposits, provident and pension funds, non-bank deposits, currency, life insurance fund, claims on government, and shares and debentures. The composition of the household sector's savings has changed over time, but the inclusion of gold in national income statistics is not advocated simply to increase the savings rate.

Ninth Plan Savings Rate

The savings rate in 1998-99 of 22.3% fell short of the Ninth Plan target of 25.2 per cent. The reliance on foreign capital and adoption of a deliberate policy to attract foreign savings into portfolio and direct investments have become a part of the liberalization policy since 1991-92. Inflow of foreign savings was to finance an investment rate of 23.4 per cent in 1998-99. While the high domestic savings of the Asian Tigers provided powerful evidence of a link between thrift and growth, relying too much on foreign capital is a danger that could give rise to an economic crisis. Mexico experienced such a crisis in 1994 where domestic savings fell on account of the substantial inflow of foreign capital in the two or three years prior to 1994, giving rise to the liquidity effect. The Asian crisis of 1997 also confirms that foreign capital especially portfolio and debt are not only undependable but also aggravate financial stress into a full. blown crisis.

All this points to the importance of strengthening thrift. The recent developments in credit financing of automobiles and white goods and the impulsive expenditure-inducing effect of credit cards-are likely to make a dent in savings.Financial sector reforms were implemented in many developing countries in Latin America and Asia as a component of a broader program of economic liberalization. While they were first introduced in the mid-1970s in Latin American countries, they gained prominence by the mid-1980s.

As a result, the savings rate in India is likely to increase.Market efficiency and savings rate, which together account for 40% of growth rate variation, are two possible explanations for India's higher growth rate, according to Jeffrey Sachs and Nirupam Rajpal of the Harvard Institute for International Development. If India increased its competitiveness to the level of other East Asian nations, Sachs and Rajpal predict that India's rate of income growth will increase to 7.2%.

Financial Obligations

Bank loans and advances make up the majority of household financial obligations, which were assessed at Rs. 26,722 crores or 1.3% of GDP in 1998-99.

Financial facilitating

The Institutions in the financial market such as Banks & other non-banking financial intermediatory undertakes the task of accepting deposits of money from the public at large and employing them deposits so pooled in the forms of loans and investment to meet the financial needs of the business and other class of society i.e., they collect the funds from surplus sector through various schemes and channelized then to the deficit sector. These financial intermediaries act as mobilisers of public saving for their productive utilization. Funds are transferred through creation of financial liabilities such as bonds and equity shares. Among the financial institutions commercial banks accounts for more than 64% of the total financial sector assets. Thus, financial intermediation can enhance the growth of economy by pooling funds of small and scattered savers and allocating then for investment in an efficient manner by using they're in formational advantage in the loan market. They are the principal mobilisers of surplus funds to productive activity and utilize this fund for capital formation hence promote the growth.

CONCLUSION

In conclusion, Indian indigenous banking is a significant and established financial system that has enhanced the prosperity of regional communities for many years. Adopting indigenous banking traditions to their full potential will help India achieve financial inclusion and empower marginalized groups as it works toward equitable and sustainable development. Policymakers and financial institutions may build a more resilient and inclusive financial ecosystem that benefits all facets of society by recognizing the value of maintaining ancient knowledge and integrating it with contemporary financial systems. Programs that promote financial literacy and awareness are crucial for enabling people and communities to make wise financial choices and defend themselves against predatory behavior. In order to sustain indigenous banking's authenticity and relevance in the shifting financial environment, it is essential to preserve and promote its cultural and ethical features.

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CHAPTER 20

SIGNIFICANCE AND COMPOSITION OF A LIABILITIES OF A COMMERCIAL BANK

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ABSTRACT:

The liabilities of a commercial bank represent the financial obligations and sources of funding that the bank owes to its customers, shareholders, and other stakeholders. This paper explores the significance and composition of a commercial bank's liabilities, including demand deposits, time deposits, borrowings, and other liabilities. It delves into the role of liabilities in determining a bank's capital structure, liquidity, and risk management. The study also analyzes the implications of different liability types on a bank's profitability, solvency, and overall financial stability. Understanding the liabilities of a commercial bank is essential for investors, regulators, and policymakers, as it enables informed decision-making and effective oversight of the banking sector.

KEYWORDS:

Borrowings, Certificates of Deposit (CDs), Customer Deposits, Interbank Deposits, Loans, Long-term Debt.

INTRODUCTION

In India, scheduled banks were created with the amendment of the RBI Act of 1935; some of these banks were previously operational as of 1881. The Allahabad Bank, the most well-known of the scheduled banks, was founded in 1865 under European control. The Oudh Commercial Bank, founded in 1881, was the first bank to be created with Indian ownership and administration. This was followed by the Ayodhya Bank in 1884, the Punjab National Bank in 1894, and the Nedungadi Bank in 1899. The 19th century therefore saw the establishment of five banks. Twelve further banks were founded between 1901 and 1914, with the Bank of Baroda, the Canara Bank, the Indian Bank, the Bank of India, and the Central Bank of India standing out.Thus, the five major banks that exist today were established before the First World War. Both in 1913 and 1929, the Indian banks experienced severe crises[1], [2].

These crises caused the failure of many banks. Bank customer trust was shaken. On banks, there was a significant rush. It's crucial to remember that although no commercial banks were founded during World War One, as many as twenty scheduled banks were created following independence, including two in the public and one in the private sectors. In 1950, four pre-existing commercial banks merged to become the United Bank of India. The Reserve Bank's second schedule contained a few non-scheduled banks[3], [4]. These factors led to an increase in the number of scheduled banks to 81. In 1968, there were 81 Indian scheduled banks; 23 of them were either liquidated, merged into, or combined with other scheduled banks, leaving 58during this point, it should be underlined that India's banking sector became known as a potent tool for influencing the speed and trajectory of the nation's economic growth during the beginning of the 20th century[5], [6]. In order to encourage the development of businesses and banking facilities throughout the nation, it was deemed necessary in 1921 to endow a State Bank with all of the government's backing and resources. The three Presidency Banks were combined to establish the Imperial Bank of India with the

goal of achieving this goal in mind. The Imperial Bank's purpose was to "extend banking facilities and make India's financial resources more accessible to trade and industry, thereby promoting the financial system, which is an undeniable prerequisite for India's social and economic development[7], [8]. Imperial Bank of India served as a quasi-central bank until 1935, when RBI was established to serve as the country's central bank and regulatory body for banks. Although it operated as a commercial bank, the government sometimes influenced its operations to control the money supply. As a result, the function of commercial banks in India has continued to be restricted to acting as a vehicle for community savings and meeting the credit requirements of a small number of carefully chosen economic sectors[9], [10].

Monetary Services

The core of our financial system is comprised of commercial banks. Millions of people, governments, and commercial entities have deposits in them. Through their lending and investment operations, they make money accessible to borrowers, including people, companies, and governments. They thereby support both the movement of commodities and services from producers to consumers as well as the monetary operations of governments. They provide a significant amount of our means of exchange and serve as the conduits for the implementation of monetary policy. These facts logically lead to the conclusion that the nation's commercial banking system is crucial to the operation of its economy. Commercial banks are crucial to our economy; in fact, without many of their services, it is impossible to see how our economic system might run smoothly. They are the core of our financial system since they can increase the country's money supply and increase buying power in tandem with the Reserve Bank of India. The financial sector's lending, investing, and associated operations support the production, distribution, and consumption processes.

The primary function of banks and other financial institutions is to serve as mediators, converting saves into investments and consumer spending. Through them, the credit demands of investors and consumers are balanced with the investment and saving needs of savers. The involvement of the banks is a must if this transference procedure is to be carried out effectively. Indeed, in carrying out their duties, they achieve significant economies of scale: the savings made available to them are used in multiple, sizable transactions tailored to the unique requirements of borrowers. They are able to save both savers and borrowers significant amounts of money by doing this instead of having to do separate business with one another.

These economies of scale, meanwhile, are not simply about saving money. Due to the extensive range of financial services, they provide, commercial banks have been dubbed "department stores of finance."

They provide a wide range of services, including money transfers, collections, foreign exchange, safe custody, safe deposit boxes, traveler's checks, merchant banking services, credit cards, gift cheques, and more, in addition to accepting deposits, loans, and investments. Commercial banks provide a range of services relating to securities. Indian commercial banks have established subsidiaries to provide services relevant to the capital markets, including recruitment banking, merchant banking, etc.

Counseling corporate clients who require capital on capital structure, source of funding, terms and conditions of issue underwriting, timing of the issue, preparation of the prospectus, and publicity for market preparation are examples of merchant banking services. While offering these services, they serve as the issue's sponsor, provide knowledgeable guidance on topics involving investment decisions, offer corporate counseling services, and offer assistance on mergers, acquisitions, and reorganizations.

Services in Fiduciary

Fiduciary Services are those that banks provide on their clients' behalf but do not appear on the bank's balance sheet. Examples include employee pension plans, provident funds, and profit-cutting initiatives handled by banks on behalf of their client companies, the Cos. In the US, banks have separate trust departments that charge a fee to handle other people's money in accordance with a trust agreement. Because banks do not own the assets held in trust, they do not appear on bank balance sheets.

Unaccounted-for Activities

For a charge, banks take on contingent liabilities like a promise to pay someone else. Another example is a stand-by letter of credit, in which a bank commits to pay a certain sum upon submission of proof of the assured party's default or failure to perform. Commercial banks in India engage in off-balance sheet transactions such as forward exchange contracts, guarantees, acceptances, and endorsement. Commercial banks' off-balance sheet exposure in 1999–2000 was Rs. 5,84,441 crores. In 1999–2000, the off-balance sheet exposure as a percentage of all liabilities was 52.6%.

Analysis Of Commercial Banks' Assets and Liabilities

A listing of the assets and liabilities of a bank is included in the balance sheet. The Banking Regulation Act of 1949's III Schedule specifies the format in which balance sheets and profit and loss accounts must be prepared by banks in India. According to the Banking Regulation Act and the Companies Act, a bank's balance sheet must be prepared in accordance with the required format and provide an accurate and fair representation of its financial situation.

DISCUSSION

Deposits

A residual term makes up the remaining portion of the liabilities to others component, which is made up of between 92 and 94% of total deposits and hardly any borrowings at less than 0.5 percent. 80–82% of the total deposits are time deposits, whereas 18–20% are demand deposits. Since aggregate deposits make up about 90% of the banking system's total liabilities and this 90% consistently adheres to the 80:20 ratio, it seems that 70% of the liabilities of the banking system have time covenants and just 20% do not.

The following headings are used to categorize a bank's liabilities:

1. Capital.
2. Fund for reserves and other reserves.
3. Deposits
4. Borrowings from brokers, other banking institutions, etc.
5. Accounts payable.
6. Other obligations.
7. Gains and losses.
8. Variable liabilities.

Receivable invoices for collections include acceptances, endorsements, and other responsibilities that belong to both parties. Consequently, they are not often seen as liabilities. To cover and expand fixed assets and business investments, to enable trading to continue and increase, to maintain depositor confidence, and to ensure viability in the face of loss resulting from unforeseen business and political fluctuation and uncertainty, particularly in an inflationary environment, all banks require capital. Reserves: A bank's reserves are another

sign of its strength. Banks are required to shift 20% of their profits to reserves in order to increase their capital base. Together, capital and reserves make up a bank's network. The reserve fund was created to cover unanticipated and unexpected occurrences. It gives the bank strength since it can tolerate significant losses. First-rate securities are held in the reserve fund.

Deposits Made by Banks

Commercial banks rely on deposits from both banks and the general public to survive. They are the main sources of bank and represent over 83% of bank liabilities. Fixed deposits, savings deposits, current deposits, contingency accounts, etc. are the many types of bank deposits. Head office money and other interbank and interbranch adjustments categorized as deposits are included in contingency accounts.

Borrowing Banking Institutions

Bills from the Bank of India were rediscounted by the Reserve Bank. Banks also borrow from other sources of refinancing, including IDBI, SIDBI, NABARD, EXIMBANK, IFC, IRBI, and other financial organizations. Bills Payable: A bank's liabilities is made up of unpaid bills. Other Liabilities: Generally speaking, they comprise inter-office adjustments, provision for dividends, unclaimed dividends, and interest provision accounts.

Balances and Cash

The component of assets that consists of cash and balances with the Reserve Bank is theoretically dependent on the Cash Reserve Ratio that the Reserve Bank established in accordance with monetary and credit policy.

Investments

The Statutory Liquidity Ratio set by the RBI in accordance with monetary and credit policy is apparently a factor in determining how the investments component is calculated.

Credit

The biggest and most significant part of the financial system's assets is credit. It is also the most complicated since, in emerging countries, it is a weapon of both agricultural and industrial policy in addition to being a result of credit policy. 90% of bank credit is made up of loans, cash credits, and overdrafts; the remaining 10% is made up of domestic and international bills.

There are off balance sheet liabilities as well, known as contingent liabilities, such as claims against the bank, guarantees and letters of credit issued on behalf of customers, liabilities on account of unfulfilled forward exchange contracts, etc.

This ratio of domestic to foreign bills has changed interestingly from 3:1 to 1:1, which is likely due to the liberalization of foreign trade as well as export finance coming under the scheme of priority sector advances.

Size

The assets and liabilities of all scheduled commercial banks as of March 2000 are shown in Table 3.1. Assets totaling Rs. 11,10,368 crores consist of Rs. 85,371 crores in cash on hand balances with the RBI, Rs. 81.019 crores in banking system assets, Rs. 4,13,871 crores in investments, and Rs. 4,43,469 crores in bank credit. liabilities of all scheduled commercial

banks are Rs. 11,10,368 crores, of which Rs. 9,00,307 crores are public deposits and Rs. 43.834 crores are reserves and excess.

Financial Centers

The Bank of England served as the model for central banking in India. The central bank's role as a banker's bank and its control over the money supply constituted the foundation of England's highly developed banking sector. The need that the banks maintain the required cash ratios was part of the central bank's role as "a lender of last resort." The British model requires an active securities market where open market transactions may be made at the discount rate in order to operate effectively. However, the success of open market operations relies on how dependent the member banks are on the central bank and how much power it has over interest rates. Later versions, particularly those in developing nations, shown that central banks serve as a government's banker, provide technical assistance in the area of foreign exchange, encourage the development of a stable financial system, and play an advising role. An increase in the cost of bank borrowing. Credit shrinkage due to a decline in credit demand.

The central bank will cut the bank rate when the economy is experiencing deflation. The opposite tendency occurs, increasing the amount of credit available to the economy. In other words, a rise in the bank rate triggers an increase in interest rates and a reduction in credit, both of which have a negative impact on investment activity and the overall economy. A decrease in the bank rate will also have the opposite impact. Money market rates decrease when the bank rate is decreased. Credit becomes more affordable. People borrow, which causes credit to expand. This boosts investment, which encourages growth in both employment and output. The economy grows gradually. The bank rate has had minimal impact in India other from serving as a harbinger of changes in the direction of credit policy. Nine changes to the bank rate occurred from 1951 and 1974, while only three occurred between 1975 and 1996. It was altered three times in 1997, four times in 1998, twice in 1999, and once in 2000. Since interest rates have been deregulated and made market-determined by the adoption of an auction method for treasury bills and government securities, it should take into effect soon. When there aren't many rates tied to the bank rate and there isn't much refinancing given to banks at this rate, changes in the bank rate aren't very significant.

Public Market Transactions

Open market operations are a better method for controlling credit than bank rate policy. Only when the bank rate policy proved to be a rather ineffective tool for monetary management did the necessity for open market operation become apparent. Some analysts believe that open market operations and bank rate policy are complementing monetary management strategies.Government securities are the major focus of open market operations, and during the busiest season, they are sold. When commercial banks sell securities and the RBI buys them, the banks' reserve positions are strengthened, allowing them to increase lending to keep up with rising demand.

Ratio of Cash Reserves

A certain portion of the commercial banks' deposits must be kept with the central bank as cash reserves. CRR was originally 5% in India. It has been raised or lowered several times since 1962, when RBI was given the authority to change it from 3 to 15 percent. Credit will expand when the CRR is lower whereas credit will decline when it is raised.

All scheduled banks, including cooperative banks, regional rural banks, and unscheduled banks, are subject to the CRR. However, cooperative banks, RRBs, and non-scheduled banks are required to maintain a CRR of only 3%, and the RBI has not yet amended this requirement. The CRR for both kinds are intended to prevent excessive speculative stock-building of commodities that are in short supply due to agricultural shortages or a decline in manufacturing output as a consequence of raw material shortages, etc. Food grains, oilseeds, jute, cotton textiles, and sugar are the commodities that these consumer goods or export-important products pertain to. These restrictions have been implemented in the form of goals to raise margin requirements, control the size of each borrower's credit limit in order to maintain a specific level of aggregate credit against a specific commodity that may be compared to the level of credit maintained during the previous corresponding period, etc. Additionally, these rules have been modified to meet the requirements of the local economy. The Reserve Bank has worked to curb excessive borrowing from the banking system via clean advances or against the security of other assets, such as shares and stocks, in addition to exerting control over bank lending against the security of certain commodities that are in short supply.

Minimum margins required for financing against certain commodities; level ceilings. a minimal rate of interest must be charged on loans made against certain commodities. The third instrument acts as leverage on the cost of credit while the first two instruments govern the amount of credit. Overall, the Indian financial sector has cooperated effectively and has a clear understanding of the necessity for such measures. The experience with India's overall efficacy has been similar to that of the majority of other nations, namely that it is comparably restricted. In general, they work best when combined with broader credit control strategies. Moral persuasion is the term used to describe the central bank's guidance or recommendations provided to banks and sometimes to other financial organizations about lending and other activities with the hope that they would execute or heed it. Moral persuasion may have a quantitative focus, such as fixing the total amount of credit that banks will offer over a certain time or advising prudence when making loans against commodities whose prices are susceptible to speculation. Letters are sometimes sent to banks requesting that they exert control over credit in general, loans secured by certain commodities, or unsecured advances in particular. With the same goal in mind, discussions with banks are also sometimes undertaken. It is easier for the central bank to secure the willing and active cooperation of commercial banks in complying with the regulatory measures, both in letter and in spirit, whenever the use of moral persuasion is possible. It also allows the central bank to exert influence not only on the borrowing banks but also on the non-borrowing banks, and other credit and financial institutions, whose operations are significant enough to affect the central bank's credit policy.

Scheme for Authorizing Credit

The Reserve Bank created the Credit Authorization Scheme in November 1965 as an additional element of credit management in the context of the Bank's strategy for containing inflationary pressures. The scheme's other primary goals were enforcing financial discipline on the bigger borrowers and making sure they did not take up valuable bank resources. To ensure that credit is used for legitimately productive purposes, that it is in line with borrowers' needs, and that there is no disproportionate channeling of credit to any one borrower or group of borrowers, the Reserve Bank regulates not only the amount but also the terms on which credit flows to the various large borrowers under the scheme.Before granting any new working capital limits of Rs. 1 crore or more to a single party or any limits that would bring the total limits that such a party was granted from the entire banking system to

Rs. 1 crore or more on a secured and/or unsecured basis, the scheduled commercial banks were initially required to obtain the Reserve Bank's prior authorization. In view of the current economic climate, the program has undergone periodic modifications. Therefore, regardless of the entirety of the credit limits made available to it by the banking system as a whole, anyloan sanctioned to a single party that exceeds Rs. 25 lakhs and is repayable over a period of more than 3 years is prohibited. This change was implemented so that borrowers couldn't get around the rules that specialized term lending institutions were trying to impose. Additionally, Reserve Bank prior approval was required before sanctioning any credit limit of Rs. 3 crores or more to any single borrower, or any limit that would bring the total limits enjoyed by such a borrower from the entire banking system to Rs. 3 crores or more on secured a loan. Public sector undertakings, including State Electricity Boards, were exempt from this requirement.

Indian Reserve Bank

The Reserve Bank of India (RBI) is the queen bee of the Indian financial system, influencing the management of commercial banks in a variety of ways through its various policies, directions, and regulations. In fact, the RBI's role in bank management is quite unique. The RBI is charged with the task of control, supervision, promotion, development, and planning.

State ownership follows private ownership

The bank's fully-paid share capital was Rs.5 crores dividend into shares of Rs.100 each; of this, Rs.4,97,80,000 were subscribed by the private shareholders and Rs.2,20,000 were subscribed by the Central Government for disposal of 2,200 shares at par to the Directors of Bank seeking the minimum share qualification. The Reserve Bank was originally established as a shareholders' bank, based on the model of leading foreign central banks of the time.

Reserve Bank of India's goals

Prior to the Reserve Bank's establishment, the Indian financial system was completely insufficient due to the inherent weakness of the dual control of currency, which is stated in the Preamble to the Reserve Bank of India Act, 1934: "to regulate the issue of Bank notes and the keeping of reserves with a view to securing monetary stability in India and generally to operate the currency and credit system of the country to its advantage.The primary objective of the Reserve Bank of India is to discharge purely central banking functions in the Indian money market, i.e., to act as the note-issuing authority, bankers' bank, and banker to government, and to promote the growth of the economy within the framework of the general economic policy of India.

In addition to performing traditional central banking duties, the Reserve Bank of India has been moving forward in carrying out a variety of developmental and promotional tasks that are typically outside the purview of a traditional Central Bank. This has been done in order to support the planned process of development of the Indian economy.

Functions

All of the conventional duties of a good central bank are carried out by the Reserve Bank of India, in addition to several tasks of development and promotion that are pertinent to the nation's economic strategy, such as:

Le. acting as a monetary authority by issuing currency notes.

1. Acting as the government's banker.
2. Serving as a supervisor and bank for bankers.

3. monetary management and control
4. Control and administration of exchanges.
5. Gathering data and publishing it.
6. Various roles and actions for growth and advancement.
7. Finance for agriculture.
8. Finance for Industry
9. Finance for exports.
10. Institutional advancement

Bank Problem

The bank has the exclusive right to issue bank notes of all denominations under Section 22 of the Reserve Bank of India Act. The Reserve Bank's notice has the following benefits:

1. It makes a note issuance uniform;
2. When there is just one organization that issues notes, credit is easy to manage.
3. It maintains public confidence in paper money;
4. It aids in stabilizing both the currency's internal and external values.

The Reserve Bank of India is required to maintain gold and foreign exchange reserves of Rs.200 crores, of which at least Rs.15 crores should be in gold. The system of note issue as it exists today is known as the minimum reserve system. The currency notes issued by the Bank are legal tender everywhere in India without any limit. At present, the Bank issues notes in the following denominations: Rs.10, Rs.20, Rs.50, Rs.100, Rs.200, Rs.300, Rs.500, Rs.1,000

1. It maintains the government's financial accounts.
2. It raises funds from the public and provides short-term loans to the government.
3. It buys and sells banknotes and currencies on the government's behalf.
4. It accepts payments and makes payments on the government's behalf:
5. It handles governmental debt and
6. It provides the government with economic advice on issues including managing public debt, price stability, and deficit finance.

Banker

The Reserve Bank of India (RBI) controls the volume of reserves of commercial banks and thereby determines the deposits/credit creating ability of the banks. Commercial banks hold a part or all of their reserves with the RBI. Commercial banks are required to keep a certain proportion of cash reserves with the Reserve Bank. In exchange, the Reserve bank offers them various facilities like advancing loans, underwriting securities, etc.

CONCLUSION

In conclusion, A commercial bank's obligations are crucial components of its financial structure, affecting the bank's risk profile, liquidity, and overall financial health. Liabilities must be managed carefully if the banking system is to remain strong and robust, promote economic development, and safeguard depositor interests.

To preserve financial stability and consumer safety, regulators must monitor banks' liability management procedures. When assessing a bank's financial health and sustainability, investors and stakeholders should take into account its liability structure as a key element. Stakeholders can support a strong and efficient banking system that promotes economic development and financial well-being by comprehending the intricacies and repercussions of

bank liabilities. The difference between the income collected on a commercial bank's assets and the interest paid on its obligations has a direct impact on its profitability.

A bank is better equipped to withstand financial market swings and economic downturns by maintaining a broad and stable liability base.

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CHAPTER 21

A STUDY ONCUSTODIAN OF FOREIGN EXCHANGE RESERVES

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ABSTRACT:

The Custodian of Foreign Exchange Reserves is a crucial role held by central banks and other financial institutions responsible for managing a country's foreign exchange reserves. This paper explores the significance and functions of the Custodian of Foreign Exchange Reserves, including the safekeeping, management, and strategic deployment of foreign currency assets. It delves into the importance of foreign exchange reserves in maintaining economic stability, supporting monetary policy, and safeguarding against external shocks. The study also analyzes the challenges and considerations faced by the Custodian in the context of global economic dynamics and evolving financial markets. Understanding the role of the Custodian of Foreign Exchange Reserves is essential for policymakers, economists, and investors, as it enables informed decision-making and contributes to the overall financial resilience and stability of a nation.

KEYWORDS:

Central Bank, Currency Peg, Dollar Reserves, Exchange, Foreign Currency, Foreign Exchange.

INTRODUCTION

The Reserve bank is in charge of stabilizing the value of the national currency abroad. The Reserve Bank maintains gold and foreign currencies as backup funds for note issuance in addition to settling unfavorable balances of payments with other nations[1], [2]. Additionally, it handles foreign money within the restrictions set by the government. Regarding the external sector, the RBI's responsibilities include the following: managing exchange reserves; administering foreign exchange controls; choosing an exchange rate system and setting or controlling the exchange rate between the rupee and other currenciesinteracting or negotiating with the monetary authorities of the Sterling Area, Asian Clearing Union, and other nations; and with international financial institutions like the IMF, World Bank, and others[3], [4].The RBI is charged with managing the investment and use of the country's foreign currency reserves in the most favorable way as it is the custodian of such funds. The RBI does this by purchasing and selling foreign currency on the foreign exchange market from and to schedule banks, who are the authorized dealers on the foreign exchange market in India. The Bank is in charge of managing investments in foreign gold reserves as well as shares and other securities issued by foreign governments, international banks, and other financial organizations.

Resort Lender

It was formerly seen to be the Reserve Bank's most significant duty. The Reserve Bank is established under the 1956 Companies Act when commercial banks fail to fulfill their depositors' responsibilities. Equity shares having varied dividend, voting, or other rights may be issued in accordance with section 86. According to Companies, bonus shares are dividends that are given in shares as opposed to cash. When reserves are capitalized, bonus shares are awarded. The balance sheet's net value is same, but shares and surplus are distributed

differently. However, the New York Stock Exchange categorizes distributions exceeding 25% as stock splits and distributions under 25% as stock dividends[5], [6].

Exchange of Shares

A share transfer is complete once the transferee's name appears in the register of members instead of the transferors. Sections 108, 110, and 111 of the Companies Act specify the process for transferring debenture shares. There are two types of transfers: transmission by operation of law and transmission under a valid document of transfer that has been properly stamped and signed by the transferor and transferee. Shares may be transferred between living parties or via a legal process[7], [8]. Both the first and second are referred to as transfers. Transfer is the legal term for a transaction. Upon the owner's death or bankruptcy, transfer takes place. Blank transfers are another way to transfer shares. It must be prepared in the appropriate format and sent to the business within the allotted window of time in order to be registered.

Preferred Stock

Nature

Compared to ordinary shares, preference shares have preferred privileges. Preference shareholders often have a preference to dividend rights. In terms of capital, it contains a preferred right to be refunded the amount of capital paid-up on such shares upon the winding up of a corporation[9], [10].

Combined and Non-Combined

There are two forms of preference shares: cumulative and non-cumulative. If there is no profit in any given year for cumulative preference shares, the arrears of dividend are carried forward and paid out of profit in the next years before any dividend is paid on ordinary shares. For non-cumulative preference shares, there is no such carry forward provision.

Participating

Such preference shareholders would be referred to as participating preference shareholders if the articles of association provide that a preference share holder would also have the right to participate in excess earnings or surplus assets on the dissolution of a corporation, or in both.

Shares of Redeemable Preferences

Redeemable preference shares are returned to the shareholder from earnings or from the money raised by fresh share issuance. Under the Companies Amendment Act of 1996, a redemption may only last a maximum of 20 years beginning on January 1, 1997. It must be made clear on the shares that they are redeemable. Redeemable preference shares are not shares in the traditional meaning of the word. They resemble debentures since they are repayable. Shares may only be redeemed in whole. When shares are redeemed using profits, a Capital Redemption Reserve Account is formed and the nominal value of the redeemed shares is transferred there. It is regarded as the company's paid-up share capital. In 1992–1993, two novel varieties of preference shares were released on the market. There are cumulative preference shares that are freely convertible as well as warrant-linked preference shares. Fully Convertible Cumulative Preference Share Equipe is divided into two parts: Parts A and B. Part A is automatically and compulsorily convertible into equity shares on the date of allotment without the need for any further action or application by the allottee, and Part B will be redeemed at par or converted into equity shares after a lock in period at the investors' discretion. The average market price is the average of the share's high and low monthly prices

throughout the six months leading up to the conversion, including the month in which the conversion would occur.Fully convertible cumulative preference share dividends must be set and limited to the fraction that corresponds to part B shares. The face value of each component of the equipe shares will decrease proportionally upon conversion, and the equipe shares will be considered redeemed to the extent of each portion on the corresponding dates of conversion.

Shares of Preference with Attached Warrants

Each preference share would have a specified number of warrants attached to it under this agreement, entitling the holder to apply for equity shares for cash at premium at any point during one or more stages between the third and fifth years after the date of allocation. The warrant holder's option to purchase the unsold share will expire if he doesn't act on it. All rights to bonus shares that the corporation may issue would be available to warrant holders. The attached warranted preference shares could not be sold for three years from the date of allocation.

DISCUSSION

Public Issues of Securities

On May 29, 1992, the Capital Issues Act of 1947, which governed the issuance of capital, was abolished. As a result, prior authorization is no longer required for the issuance of capital by corporations or the price of their issues.

The Securities and Exchange Board of India has, however, set certain rules for the observation by the firms making issuance of capital in order to guarantee adequate disclosure and investor protection. The rules include the criteria for new and current private/closely owned firms' first capital issuance as well as subsequent capital issues by other companies in the form of shares, debentures, and bonds. The rules will be applicable to all capital offerings.

Keep Over-Subscriptions

Whether it is a rights issue or a public offering, the amount of the issue cannot be more than what is stated in the prospectus or letter of offer. Lead Merchant Banker to Name Compliance Officer The lead merchant bankers should name a senior officer as the compliance officer to make sure that all rules, regulations, guidelines, notifications, etc. issued by SEBI, the Government of India, and other regulatory bodies are followed. The Compliance Officer is responsible for internal compliance as well as coordination with regulatory bodies on a variety of issues.

The compliance officer must also make sure that any flaws mentioned by SEBI are not repeated.

SEBI Public Issues Guidelines

Securities Offering Through Offer Document Eligibility Requirements

Only after submitting a draft prospectus via a merchant banker to SEBI and filing it with the Registrar of Companies 21 days beforehand can securities be issued publicly. Before submitting your prospectus to ROC, you should include any changes that SEBI specifies.

If the letter of offer is not filed with SEBI through a merchant banker at least 21 days before the offer is filed with the regional stock exchange, rights issues by listed companies for Rs. 50 lakhs plus premium cannot be done.

Dematerialization

The corporation should make arrangements for the dematerialization of securities that have already been issued or that are scheduled to be issued before a public offering, a rights issue, or a sale of securities. Investors should have the choice between receiving share certificates and holding them digitally.

Public Offering of Securities by a Company

1. It must have pre-issue net worth of Rs. 1 crore in three of the five years before, with a minimum net worth requirement being satisfied in the two years prior; and

2. It has a history of distributing earnings for at least three of the five years just before. An unlisted firm that does not fulfill the minimum net worth and track record requirements should employ the book-building approach for the public offering of securities. The issue size should not exceed five times the issuer's pre-issue net worth, and 60% of the issue should be allocated to qualified institutional purchasers. Offer to Buy

Company Listed Public Issue

Issue size shouldn't be more than five times the value of the last issue. If the issue size exceeds five times the net value of the issue, a book building method must be used. 60% of issues throughout the book-building process ought to go to QIBs. Banks, infrastructure businesses, and rights issuance by publicly traded corporations are exempt from the rule.

Debt Instrument Credit Rating

1. No public offering of debt instruments, regardless of maturity duration, may be done without first obtaining and disclosing a credit rating.
2. All credit ratings, even rejected ones, must be provided when credit ratings are acquired from several agencies.
3. Two ratings from two agencies must be acquired for debt instruments with public and rights issuance totaling more than Rs. 100 crores.
4. Any listed security's previous ratings from the three years before must be stated in the offer document.

When a Security is Convertible

The promoter may, at his discretion, invest in equity convertible securities, provided that a minimum 20% contribution is made overall.

When a promoter's involvement exceeds the necessary minimum percentage in a listed firm, the price clause of the guidelines on preferential allotments applies. Contributions from the promoters must be received before the public issue is made. At least one day before the opening date, the whole contribution, including the premium, should be brought in. A resolution granting shares or convertible debentures to promoters must be approved by the company's board of directors.

The resolution must be submitted with SEBI, together with a certificate from a Chartered Accountant attesting to the inclusion of the founders' contribution.

Exemption from the Promoter Contribution Requirement

if the listed firm has a history of paying dividends for the three years prior. when no recognizable promoter or promoter group quits a company; and when a rights dispute occurs.

Minimum Lock-in Requirements for Public Issues

For a period of three years, the minimum promoter contribution is fixed.

Locking in of Extra

The surplus would be locked in for a year in the event of a public offering by an unlisted firm as well as a listed company. An unlisted company's pre-issued share capital must be locked in for a full year. Pre-issue share capital held by venture capital funds and overseas investors who are registered with SEBI and who have held the capital for at least a year at the time the offer document is filed with SEBI and made available to the public for purchase is not covered by this.

Based on Firm Allotment

For one year after the start of commercial production or the date of allocation, securities issued on a firm allotment basis are locked in. Securities that are locked in should include a statement stating their tenure and that they are not transferable.

The Lead Merchant Banker's obligations

Diligent Effort

The lead merchant banker should be confident in the completeness and appropriateness of the information in the offer papers. Even after the issue procedure, he would still be liable. He should submit the draft offer paper to SEBI along with the required payment. Documents to be Submitted Along with Offer Document The offer document should be submitted to SEBI along with the memorandum of understanding between the lead merchant banker and the issuer firm outlining their respective rights, responsibilities, and duties in relation to the issuance.

Charges associated with intersex allocation

The rights and obligations of each merchant banker are defined if the issue is handled by more than one merchant banker.

When subscribing

The lead merchant banker in charge of the underwriting arrangements should impose underwriting obligations, make sure that the underwriters pay the development amount, and ensure that this information is included in the interest allocation of responsibilities that is submitted with the lead merchant banker's due diligence report to SEBI.

Others

Verify that the offer document has been updated to include any SEBI recommendations, revisions, or remarks. At the time the prospectus is filed with the Registrar of Companies, provide a new certificate attesting to your company's diligence. Provide a new certificate attesting that no corrective action is required on your part. Provide a new certificate after the issue has opened but before it closes for subscription. Provide a new certificate signed by a company secretary or chartered accountant in the case of listed companies making additional capital offerings.

Along with the draft offer paperwork, the lead merchant banker must also provide the aforementioned certifications, each of which must be officially signed by a company secretary or chartered accountant.

Undertaking

Promoters will record any transactions in securities they make within 24 hours after submitting a document with the ROC-SE and the closing of the issuance.

Release of Offer Document to the Public

Within 21 days of the day, they were filed with SEBI, offer materials must be made available to the public. Lead merchant banker is responsible for seeing that the offer papers are lodged with the stock. exchange where it is intended to list the securities. Additionally, the offer document must be submitted to SEBI. The co-lead manager has 15 days to secure and provide SEBI with the stock exchange's principled approval for listing the securities.

Transmission of Issue Material

For public offerings, the lead merchant banker must make sure that the offer paperwork and other issue materials are sent to the appropriate stock exchanges, brokers, underwriters, issue bankers, and investors' associations in advance as agreed. The lead merchant banker must make sure that the letters of offer are sent out one week before the issue is opened in the event of rights offerings.

Certificate of No Complaints

The lead merchant banker is required to submit to SEBI a list of complaints it has received within 21 days from the day the draft offer document was made public, update the draft offer document, and underline those revisions.

Centers for Mandatory Collection

The four metropolitan hubs in Mumbai, Delhi, Calcutta, and Chennai, as well as all other such locations where the stock market is situated, are the minimal number of collecting centers for the issuing of capital.

Agents of Authorized Collection

In collaboration with lead merchant bankers, whose names and addresses shall be included in the offer document, the issuer business may identify collection agents.

Lead merchant banker must make sure that money order and infrastructure are available for collection agents to use. They gather applications that are supported by check payments, drafts, and stock invoice collections, all of which are sent to Registrars for the Issue.

Advertisement for Post-Issue Rights

The lead merchant banker is responsible for making sure that, in the event of a rights issue, an advertising that includes the date that the letters of offer were completed and sent out is published at least seven days prior to the issue's opening date.

Making a Compliance Officer appointment

The issuing corporation has to establish a Compliance Officer who communicates with SEBI directly about adhering to the agency's many laws, rules, regulations, and other directions. SEBI should be made aware of the compliance officer's name.

Underwriting

Security issues are underwritten to assure that, in the event of undersubscription, the underwriters will pick them up. Although merchant bankers and stock brokers registered with

SEBI do not need separate registration, no one may serve as an underwriter without first getting a certificate of registration with SEBI. At the end of March 2001, there were 56 registered underwriters with SEBI in addition to merchant bankers and stockbrokers. Financial institutions from all throughout India, commercial banks, merchant bankers, and stock market members are major underwriters. Underwriting is organized by the Lead Manager in cooperation with the business.

Financial stability is a key factor when choosing an underwriter. A contract known as a "underwriting agreement" is made between the firm providing capital and an underwriter, who is typically a merchant banker or financial institution like UTI, other mutual funds, LIC, or ICICI. According to the agreement, in the event that the issue is not completely subscribed, the under writers undertake to subscribe to or secure subscription to a part of the capital to be issued. Such help as well as ready aid with regard to rights issues. The underwriters' maximum responsibility is limited to the sum that he underwrote.

SEBI Regulations

Since October 1994, SEBI has made underwriting optional for offers to the public with the caveat that the full amount collected would be returned to investors if the issue was not underwritten and failed to raise 90% of the amount offered to the public. Regulations for capital issue underwriters were issued in October 1993.

One of the crucial rules was that the underwriters had to register with SEBI, among other things. An underwriter must have a minimum net worth of Rs. 20 lakhs in order to register.

Total debt owed by underwriters at any one moment shouldn't be more than 20 times their net worth. The risk of sub-underwriting is assumed by the underwriters.

Variable Underwriting

It is known as contingent underwriting when underwriting commission is only paid on the amount devolving. In the prospectus, specifics of the underwriting agreement should be stated.

Public Concern through Prospectus

The prospectus is the most popular way to offer securities to the public. 10,528.7 crores, or 71.4 percent, of the Rs. 16371.2 crores in fresh capital issuance made in 1995–1996 were done so through prospectus.

The rights issuance represents a significant chunk of debentures. 87.7% of the Rs. 5,692.2 crores in fresh capital offerings in 2001–02 were done through prospectus. Prospectus accounted for 99.7% of equity issuance, while rights to convertible debentures made up 86.4%.

Initial Public Offerings Study Area

Business Line conducted research of the 625 initial public offerings (IPOs) that were listed on the BSE in 1996.

There were both par and premium offers in the IPOs. The research included comparisons between the offer price, the listing price, and the most recent traded price. Premium Officers In 1996, only 20 of the 92 premium offers placed on the BSE offered returns more than 20 percent upon listing. The average gains were 8% upon listing, 2% at the conclusion of the relevant listing month, and 14% on the last trading day.

Lesser Offers

In 85.28 % of the sample consisted of Par Offers. A return of 35% was provided by Par Offers on the listing. However, on the last trading day for the study's purposes, 80% of the quotes were for the offer price. If you include all the firms, including par and premium, 530 issues had annualized returns of less than 20% at its most recent pricing, while 95 had returns more than thatissuing of Prospectus, The Companies Act's Sections 55 to 68 A address the issuing of prospectuses. The prospectus outlines the company's prospectus as well as the reason cash is needed. The definition of a prospectus in Section 2 states that it includes any notice, circular, advertising, or other document that solicits public offers or deposits in exchange for the subscription or purchase of any shares in or debentures of a body corporate. If a document does not invite the public to subscribe for shares or debentures of a corporation, it is not a prospectus.

Requirements and Transparency in Prospectuses

As a result of the committee's recommendations, which were made under Shri. Guidelines were released by Y.H. Malegam in September 1995, among other things, to address increased transparency in the draft prospectus submitted to SEBI and to requirements in prospectuses submitted to SEBI for review. Copies of the draft document must be concurrently filed by the lead merchant banker with the stock exchanges where the issuance is planned to be listed.

Prospectus's Date

A prospectus must be published on the specified date, which must correspond to the desired firm. The directors or their designated representatives must sign it.

Filing of a Prospectus

A copy of the prospectus must be sent to the registrar of companies before it may be issued. Before publishing, registration is required. The copy of registration must be accompanied by the following documents: written statements relating to any adjustments to profit and loss, assets, and liabilities; consents of the auditor, legal advisor, attorney, solicitor, bankers, and broker of the company to act in the capacity; copies of all significant contracts, excluding those entered into in the ordinary course of business; copies of every material contract.

CONCLUSION

In conclusion, the financial stability and economic health of a nation are crucially protected by the Custodian of Foreign Exchange Reserves. A vital line of defense against external economic threats, foreign currency reserves also support investor confidence. Maintaining enough reserves, maximizing profits, and adhering to reliable risk management procedures all need careful balancing in order to manage reserves effectively. Policymakers and financial authorities may make choices that support the overall resilience and stability of the country's economy by having a clear knowledge of the duties and difficulties the Custodian faces. Investors and market players may learn more about how foreign currency reserves are strategically used, which can have an impact on the dynamics of the world's financial markets and investment choices.

The Custodian may make sure that foreign currency reserves play their vital part in promoting economic success and financial stability by ensuring openness, accountability, and sound management practices. Additionally, clear and understandable communication with key parties, such as government authorities, central bank officials, and the general public, is crucial for ensuring reserve management standards.

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CHAPTER 22

EXPLORES THE NATURE AND SCOPE OF VENTURE CAPITAL

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ABSTRACT:

Venture capital (VC) is a form of private equity financing that involves investing in early-stage, high-potential startups and small businesses with the expectation of significant returns. This paper explores the nature and scope of venture capital, examining its unique characteristics, investment criteria, and role in fostering innovation and entrepreneurial growth. It delves into the various stages of venture capital funding, from seed financing to exit strategies, and the risks and rewards associated with VC investments. The study also analyzes the impact of venture capital on economic development, job creation, and technological advancements. Understanding the nature and scope of venture capital is essential for entrepreneurs, investors, policymakers, and researchers, as it enables informed decision-making and facilitates the cultivation of a vibrant entrepreneurial ecosystem.

KEYWORDS:

Angel Investors, Equity Investment, Funding, High-risk,Initial Public Offering (IPO).

INTRODUCTION

Technocrats with innovative, high-risk enterprise plans might get help from venture capital firms or businesses by using merchant hankers.

An essential source of funding for technology-based firms that considerably aid in the development process is venture capital. Such green filed enterprises cannot use public concerns.

In order to support the expansion and success of growth-oriented businesses, venture capital refers to structured private or institutional finance that may contribute significant sums of cash, mostly via stock acquisitions and sometimes through debt offers.

Institutional investors who finance startup companies with equity and actively advise their management are referred to as venture capitalists[1], [2].

Indian venture capital

VC funds are a component of the main market. Apart from one overseas venture capital company, there are 35 venture capital funds registered with SEBI. According to data available for 14 enterprises, they had a total of Rs. 1402 crores in funds on hand by the end of 1996, of which Rs. 672.85 crores were allocated to 622 projects.

The term "private equity" has replaced the initial restriction on venture capital to risk capital. Venture capital refers to money invested in risky but high-return new businesses. VCFs provide equity financing for businesses that plan to use cutting-edge technology and are run by skilled and knowledgeable entrepreneurs.

Additionally, they provide managerial, financial, and technological support and aid in the establishment of the company's reputation. VCF may sell its shares in the firm after it fulfills the OTCEI's or the stock exchange's listing standards[3], [4].

Venture Capital Characteristics

The three main characteristics of venture capital funds that make them particularly suitable as a source of risk financing are as follows: that it is a long-term, active kind of investment; an equity or quasi-equity investment; and an active form of investment. First, since the investor takes on risk, venture money is equity or quasi equity. For his investment, there is no security. The practice of taking risks is institutionalized by venture capital, which supports the creation of successful domestic technology.Second, venture capital is a kind of long-term investing that requires both cash and time[5], [6]. Finally, venture capital investment entails involvement in the company's management. A venture investor serves on the board and advises the company on strategic and administrative issues. Financing new and quickly expanding businesses, buying equity shares, helping to turn innovative technology-based ideas into products and services, adding value to the company through active participation, taking risks in the hope of big rewards, and having a long-term outlook are all characteristics of venture capital. These characteristics make venture finance perfectly suitable as a source of risk funding for homegrown technological advancements[7], [8].

Indian stock markets

Stock exchanges are the best sort of market for securities, including shares and debentures issued by joint-stock corporations as well as securities of government and semi-government agencies and other public organisations. Share buying and sales are carried out in a free market environment on the stock market. Over-the-counter sales and acquisitions of government securities occur outside of the trading ring. The fundamental rules of supply and demand dictate the fairest pricing at which deals are done in the trading ring by participants in stock exchanges[9], [10].

Stock Exchanges

The only stock exchanges in operation throughout the 19th century were those in Mumbai (1875) and Ahmedabad (1894), both of which were established. These were established as voluntarily non-profit broker organizations to control and safeguard their interests. The Mumbai Securities Contracts Act of 1925 used to govern dealing in securities until the control of securities became a fundamental issue under the Constitution in 1950.

The Mumbai Stock Exchange and Ahmedabad were both recognized under this Act in 1927 and 1937, respectively. Several stock exchanges were established during the golden boom, even in Mumbai, Ahmedabad, and other centers, but they were not recognized. Soon after it was declared a Central issue, legislation was presented at the Central level, and a committee under the leadership of A.D. Gorwala worked on the Securities Regulation Bill. In 1956, the Securities Contras Act was enacted as a result of public debate and the committee's recommendations.Any organization or person, whether incorporated or not, created for the purpose of aiding, regulating, or managing the business of buying, selling, or dealing in securities is referred to as a stock exchange. For the goal of self-regulation and defending the interests of its members, it is an organization of member brokers.Only if it is approved by the government in accordance with the Securities Contracts Act of 1956 may it be used. The recognition is given by the Central Government, Ministry of Finance, Stock Exchange Division in accordance with Section 3 of the Act.The Act grants the Central Government a wide range of powers, including the following in particular:

1. The granting and revocation of recognition, permission, or bylaw amendment.
2. Request recurrent payments from the Stock Exchange.
3. Make direct inquiries about the Stock Exchange or the members.

4. The Exchange's obligation to produce yearly reports.
5. Ordering the Stock Exchange to adopt certain regulations.
6. Replace the Exchange's Governing Board.
7. Dissolve the Exchange's Governing Board.
8. Place any further restrictions or guidelines on trade.

Byelaws

In addition to the aforementioned Act, the Securities Contracts Rules were also established in 1957 to control certain aspects of trading on stock exchanges. The Exchange has its own bylaws as well, which cover the following topics. Opening and closing of the stock exchange, timing of trading, control of the settlement and other Stock Exchange activities, fixation of margins, fixation of market prices or making up prices, regulation of taravani business, etc., regulation of brokers' trading, brokerage, trading rules on the Exchange, arbitration and settlement of disputes, settlement and clearing of the trading, etc.

Control over Stock Exchanges

The Securities Contracts Act serves as the framework for how India's stock exchanges operate. Without authorization or recognition from the government, no exchange may lawfully function. Under Section 19 of the aforementioned Act, stock exchanges are granted a monopoly in a certain sector in order to simplify oversight and regulation. If certain requirements are met and the government receives the required data, recognition of a stock exchange may be given. If necessary, recognition may also be withheld. In areas without stock exchanges, the government may provide licenses to selected brokers to act as the exchange's agents.

Governmental

As previously mentioned, a Stock Exchange is only authorized if the government is satisfied that its Rules and Byelaws comply with the requirements set out for maintaining fair transactions and investor protection. The following cities have received permanent recognition to date: Mumbai, Calcutta, Delhi, Chennai, Ahmedabad, Hyderabad, Bangalore, Indore, etc. The government must also be convinced that granting such recognition would be in the best interests of the industry and the general public. On sometimes, momentary acknowledgment is given to others.

The rules of a recognized stock exchange pertaining to the Exchange's general structure, the governing body's management powers, its constitutions, the admission of members, the requirements for membership, the expulsion, suspension, and readmission of members, the registration of partnerships, and the appointment of authorized representatives and clerks must be duly approved by Government. Only with the prior consent of the government are these regulations subject to amendment, modification, or revocation. Government approval is also required for the bylaws of authorized exchanges, which specify the regulation and control of securities contracts as well as every part of members' trading operations, as well as for any adjustments or alterations. Any regulations or byelaws of a registered stock exchange may be made or amended Suo moto by the government if it deems it necessary in the benefit of commerce and the general good.The Act gave the government even more draconian powers, including the ability to investigate the activities of a recognized stock exchange and its members, take control of the exchange's assets, suspend operations, and, in the event that such action is deemed necessary for the good of commerce and the public interest, revoke the recognition that exchange has been granted. As a result, the government has exclusive authority over the established stock markets.

DISCUSSION

Licensed Dealers

Government regulation of the stock market is implemented via the recognized stock exchanges. The Securities Contracts Act of 1956 gives the government the authority to issue licenses to dealers in securities when there are no stock exchanges. These authorized dealers are currently working for the OTCEI and NSE.

1957 Securities Contracts Rules

The Securities Contracts Rules, 1957 have been published by the government in accordance with the Act to carry out the legislative intent. These regulations outline the steps that must be taken for stock exchanges to be recognized, including periodic returns and annual reports from recognized stock exchanges, inquiries into the operations of recognized stock exchanges and their members, and specifications for the listing of securities. The regulations are legislative and provide a set of common standards that apply to every registered stock exchange.

Recognized Stock Exchanges at the Moment

The stock exchange functions as an organized market for securities and operates under the rules, bylaws, and regulations that have been properly recognized by the government. For many different reasons, they provide the most ideal kind of market. Purchases and sales are done under the circumstances of free and perfect competition thanks to active bidding and, in the case of shares and debentures, two-way auction trading. Members of the exchange negotiate deals at the fairest price as defined by the fundamental rules of supply and demand. As a result, even while shares and debentures of joint-stock corporations reflect interest in industrial property, such as mills and factories, machinery, and equipment, gilt-edged securities indicate ownership of public debt. As a result, they become the most liquid of assets and are capable of being readily bargained.

Requirements for Membership

Members of recognized stock exchanges should meet the requirements listed below:

1. Age 21, Indian national, clean record.
2. Not added to the debts owed to creditors.
3. Not found guilty of fraud or deceit.
4. Not working as a broker or agent for any other company.
5. Education requirements should be 10 plus 2.
6. Unaffiliated with any business or entity.
7. Has never defaulted on a stock exchange.

According to the previous regulations, businesses and financial organizations are not members. However, the government has approved a revision to the exchange's bylaws that will allow for corporate and institutional members as well as authorization for a member of any stock exchange throughout 1993–1994. Contracts with parties other than other members or dealing with clients as principles are not permitted for members. Spot delivery transactions are not subject to the Act's restrictions.

Only members in the designated locations where the stock exchange is located may pass contracts. If the sub-brokers are registered with SEBI, they may also transmit legitimate contract notes or confirmation.

Organization

While the Calcutta, Delhi, Bangalore, Cochin, Kanpur, Ludhiana, Guwahati, and Kanara Stock Exchanges are joint-stock companies limited by shares and the Mumbai, Hyderabad, and Pune stock exchanges are companies limited by guarantee, the recognized stock exchanges at Mumbai, Ahmedabad, and Indore are voluntary non-profit associations. There is a great deal of standardization in the way recognized stock exchanges are set up since the Central Government has approved the Rules or Articles of Association outlining their organizational structure. In reality, as a prerequisite to its registration by the Government of India, the Chennai Stock Exchange was reconstructed and the Calcutta Stock Exchange had to go through a significant restructuring.

Controlling Body

A recognized stock exchange's governing body, which also serves as the decision-making body, is endowed with extensive political and administrative authority. It has the authority to establish, revise, and suspend the operation of the exchanges' rules, bylaws, and regulations, subject to governmental approval. Additionally, it has full authority over each and every member, and in actuality, its management and control authority are almost total. According to the constitution, the governing body has the authority to admit and expel members, warn, censure, fine, and suspend members as well as their partners, attorneys, remisiers, authorized clerks, and employees; to approve the formation and dissolution of partnerships; to appoint attorneys, remisiers, and authorized clerks; to enforce attendance and information; to resolve disputes; to set the terms and conditions of stock exchange business; and to resign. The Mumbai Stock Exchange is run in a standard manner. A President, Vice-President, and Treasurer are chosen by the 16 members of the Governing Board who are elected by the members on the register. On the Governing Board's suggestion to the Chief Administrator of the Exchange, the government appoints the Executive Director. On the Board, their interests are also represented by three members from the government, three from the general public, and one from the RBI. According to SEBI regulations, the Exchange has committed to provide non-members a 50% participation on the Governing Board.

Activities of the Stock Exchange

Liquidity is offered by stock exchanges to listed corporations. They facilitate trade and generate money from the market by providing quotes to the listed firms. Because of this easy marketability and unparalleled capability for transfer of ownership of stocks, shares, and securities given by the authorized stock exchanges, savings of investors pour into public loans and to joint-stock businesses. In turn, over the 120 years that the stock exchange has existed in this nation, and through their medium, the Central and State Government have raised crores of rupees by issuing public loans; Municipal Corporations, Improvement Trusts, Local Bodies, and State Finance Corporations have obtained from the public their financial requirements; industry, trade, and commerce - the foundation of the nation's economyhave secured capital of crores. Companies were able to raise more money and attract public investment by getting the listing and trading capabilities. The listed corporations with high public interest have benefited in certain ways, and asset appraisal for tax and other reasons has become simpler.The secondary market rapidly increased throughout the 1980s, keeping pace with the development in new issues. There were 24 stock exchanges in total in 1996, including the Visakhapatnam Stock Exchange, which was established in that year, up from 8 in 1980. By the end of 1995, there were around 6,000 members of the stock market, up from approximately 1,200 a decade earlier. Over 8000 firms were listed on all stock exchanges in 1995, of which 6500 are listed on B.S. Exchange. In the 1980s, the market capitalization also

saw a significant surge. Over the last 10 years, the amount of everyday trading has multiplied more than ten-fold. There were up to 1.53 lakh transactions completed each day.

Capital Listed Paid-Up

The paid-up share capital of publicly traded firms was Rs. 270 crores in 1946 and over Rs. 1,05,284 crores in 1996. The market value of these listed businesses' capital was around Rs. 5.5 lakh crores in 1995; this value decreased to approximately Rs. 3.5 lakh crores owing to a severe decline in prices in 1995, but increased to 4.77 lakh crores in December 1996.

Premier Exchange in Mumbai

The top stock exchange in India is the Mumbai Stock Exchange. In 1957, it became the first to get official recognition. The capital listed in Mumbai made up around 40% of the total capital listed on all stock exchanges, but it held roughly 90% of the market capitalization. Mumbai came in top place for both the overall number of listed firms and stock issuance. Although comparable data for other exchanges is sometimes unavailable, the Mumbai Stock Exchange routinely provides figures on market turnover of securities. However, it is widely estimated that the turnover of the Mumbai Stock Exchange accounts for 60% to 70% of the total turnover of all the stock exchanges in the nation. As a result of NSE taking the lead in daily trading turnover, however, the proportion of BSE has decreased to less than 50%.More than 8,000 firms were mentioned on the stock markets, 6,500 of which were listed in Bombay. The number of transactions completed during the five-hour session at 10 a.m. on the Mumbai Stock Exchange. to 3.00 p.m. about 1,50,000. Between Rs. 300 billion to Rs. 700 billion is the daily turnover.

Pattern of Trading in the Stock Market

The remaining mentioned securities are grouped together. In 1996, there were 3,500 firms that were routinely listed on the BSE, 6,500 total scrips, and 90% of them were equity-based enterprises. Only roughly 3,000 of these equity shares or companies are traded on a daily basis. The remaining items are not traded in at all. To offer liquidity to Group once every two weeks or once on Saturdays, only odd lots are traded. The approved securities, often known as foreign securities since they are listed on other stock exchanges in India, are those that are not listed on the Exchange but are allowed to be traded on this Exchange. Equity shares, preference shares, debentures, CCI's PSU bonds, and government securities are the trading instruments.

Commerce and Settlement

Genuine Investors vs. Speculative Traders

There are two types of stock market investors: legitimate investors and speculative investors. The former does not intend to engage in carry-forward activity when they receive and distribute shares. The latter, however, simply deal with disparities in buy and sell prices and neither provide nor receive delivery of shares.

Even if they accept delivery, their goal is to profit from price discrepancies between the buy and sell.

Genuine investors are motivated by long-term rewards. Any sincere investor who buys and sells with delivery may see short-term profits of a few months. The purpose to accept and provide delivery of shares or to simply carry forward and profit from disparities distinguishes these two kinds.

Speculators' types

Depending on their activities and areas of expertise, there are several classifications of brokers on the stock markets. A broker essentially acts as a middleman between buyers and sellers of securities. His clientele might include people, businesses, trusts, charities, etc., as well as banks and other financial organizations. Some of these customers can be traders who deal in pricing discrepancies and conduct commerce to continue ahead. Second, wholesalers that purchase and sell in certain scrips are known as jobbers of Travails. For the scrips they trade in, they provide both the bid and the offer prices.

They resemble market-makers in other countries' marketplaces. Thirdly, there are baitwells who provide the finance for carry-forward transactions and lend securities as needed. The blank transfer of T.D.s with shares facilitates such carry-forward or badli transactions. These blank transfers are transfers that have not had the names of the transferees added to them, nor do they need the payment of any stamp duties or other fees.

Bulls and bears are the two primary groups of speculators on the stock market. Tejiwallas who acquire stocks with the intention of selling them for a profit are known as bulls.Mandiwallas, or bears, are those who sell stocks in anticipation of a decline in price and then repurchase them at a later time. Stags are members who don't purchase or sell but instead subscribe to fresh issues in the hopes of eventually selling them for more money after they are listed on the stock market. So, the following is a breakdown of what brokers do. In the Primary Market, one can take on the roles of a dealer, broker, jobber, etc. in the trading ring, badla financier for carry-forward business, arbitrageur buying and selling as between the various markets, such as in Mumbai and Delhi, dealer in government securities, bonds, etc., adviser, consultant, and portfolio manager, among others.

Allied Services

Investor services such as home delivery of shares, arranging for transfers of shares, safekeeping of shares, etc.; dealing in inter-corporate investments to function as broker for fixed deposits of corporations; operating in the money market; PSU bonds, UTI units, Mutual Fund Schemes, etc.; and dealing in PSU bonds, UTI units, and other PSU-related securities.

The Broker's Fees

Except for the chari trusts, the broker bills all customers for brokerage after the purchase or sale is completed and at the time the contract note is transferred. The brokerage, which may be anywhere between 0.5 and 2.5%, is not paid separately but is included in the price.

Shipping Payment

In a buy transaction, the broker initially accepts the check for the purchase before delivering the shares. In exchange for a selling transaction, he subsequently pays by check but first accepts delivery of the shares.

This is explained by the stock exchange's settlement process, which established the delivery and pay-in dates first. Each member must first give shares or pay money to the clearing house. The clearing house pays by check and distributes the shares to the members on a later day designated for payment.

These members' transactions with the clearing house can only be completed when their customers, in turn, pay in first, submit the checks, deliver the shares, and then get the checks from them, or receive the shares later on the pay-out day.

Settlement Methodology

To understand why such delays, occur, it is necessary to know the stock exchange's settlement process. For each settlement, there will be 5 to 15 trading days, and then three days will be set aside for carrying forward and squaring up. The Exchange's Settlement Committee sets the timetables. One or two days will be set out for fixing mistakes and omissions and ensuring a final agreement on each member's viewpoint with regard to the other members on all scrips. The net position is arrived at by accounting for both sales and purchases scrip-wise, and the payment to be paid or received is then decided upon. Then, a pay-in day is established for those who are required to contribute to bring checks or shares to the clearing house. To assist settle any outstanding payments, there will be a first pay-in-day and a final pay-in-day after a few days. Finally, a specific pay-out date is established with a one-to-two-day window for the clearing house to complete all payments or share deliveries to members.

Auctions

For scrips that were unable to be supplied even on the last day, auctions were set up. The auctions are offers to acquire the required scrips in the amounts that have been ordered but not yet received, allowing for delivery to the purchasers. When the seller doesn't deliver on the scheduled day and, in the case of group B, at the buyer's request, auction in group A is automatic. The stock exchange organizes auctions by calling for bids from members to purchase the shares on behalf of the member who was unable to deliver the shares.

Cleaning Method

Each day once trade is finished, members submit their saudas to the exchange. If there are any complaints or revisions the next day, these are filed as wandha memoranda. Throughout the five to ten trade days, this procedure occurs every day. These memoranda are entered into the computer, which then calculates the daily net position. Any margins imposed by the stock exchange authorities are collected from members and placed in the clearing house. The final net position of a member is determined after taking into account all of their transactions, both squared up and to be carried forward. Members' squaring up positions and carry forward positions are known on the three days designated for badla settlement. Any complaints or errors are noted, and the necessary repairs are made. The initial corrected position of the members is then established. The carry over margins, if applicable, are now collected. This serves as the rationale for requesting that members deliver or pay for their shares on the pay-in day. Due to the high trading volume and the significant amount of speculative trading and carry forward transactions on the BSE, the complete procedure takes between 30 and 60 days.

CONCLUSION

In conclusion, Venture money is essential for fostering creativity, promoting entrepreneurship, and spurring the economy.

It serves as a catalyst for innovative concepts and technical developments because to its nature, which is characterized by risk-taking and early-stage investments. Entrepreneurs and investors must carefully assess possibilities and manage risks as venture capital continues to alter sectors and economies.

By putting supporting laws and regulations into place that promote entrepreneurship, draw funding, and create an atmosphere where companies may thrive, policymakers can help venture capital succeed. Stakeholders may collaborate to establish a resilient and dynamic entrepreneurial ecosystem that fosters growth, produces employment, and brings wealth to

society as a whole by comprehending the nature and scope of venture capital. But venture capital also has to contend with issues including transaction flow, portfolio company management, and executing effective exit plans. To promote a flourishing startup ecosystem, governments must work to create a climate that is favorable to venture capital and entrepreneurial activity.

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CHAPTER 23

ANALYZES THE BENEFITS AND CHALLENGES ASSOCIATED WITH FOREIGN DIRECT INVESTMENT

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ABSTRACT:

Foreign Direct Investment (FDI) is a key driver of global economic integration and plays a pivotal role in facilitating cross-border capital flows and international business expansion. This paper explores the nature and significance of Foreign Direct Investment, examining its various forms, determinants, and impacts on host and home countries. It delves into the motivations behind FDI, including seeking new markets, accessing resources, and leveraging comparative advantages. The study also analyzes the benefits and challenges associated with FDI, including its potential to boost economic growth, enhance technological transfer, and create employment, while also raising concerns related to sovereignty, income inequality, and potential market distortions. Understanding Foreign Direct Investment is essential for policymakers, investors, and business leaders, as it enables informed decision-making and contributes to the formulation of effective policies to harness the potential benefits of FDI and manage its associated risks.

KEYWORDS:

Capital Flows, Developing Countries, Economic Development, Equity Participation, Foreign Direct, Host Country.

INTRODUCTION

In 1991, there was a liberalist approach to foreign investment that allowed for automatic acceptance of foreign investments up to 51 percent ownership in 34 sectors. In 1996-1997, thirteen new sectors were established, with three of them enabling equity involvement up to 50% and nine priority sectors with an increase in the equity ceiling to 74 percent permitting automatic approval[1], [2]. The Foreign Investment Promotion Board was established to handle applications in circumstances when automatic approval is not applicable[3], [4]. To encourage foreign direct investment in India, the Foreign Investment Promotion Council and the FIPB were formed on July 22, 1996. Additional initiatives, including direct foreign investment, portfolio investment, NRI investment and deposits, and investment in global depository receipts, were implemented to promote investment flows throughout the 1992–1993 period. The measures' specifics are:

1. With the exception of the consumer goods industry, the dividend balancing requirement that used to apply to foreign investment up to 51 percent ownership is no longer relevant.
2. Existing businesses with foreign stock may increase it to 51 percent under certain regulated conditions. The discovery, production, and refinement of oil have also been opened up to foreign direct investment [5], [6].
3. With reparability of capital and income, NRIs and foreign corporations that are mostly controlled by them are also allowed to invest up to 100% of their shares in high-priority sectors. Additionally, NRI investments up to 100 percent of equity are permitted in export houses, trading houses, star trading houses, hospitals, EOUs, sick industries, hotels, and tourism-related businesses, as well as in the hitherto prohibited

sectors of real estate, housing, and infrastructure, without the right to compensation. The Reserve Bank of India no longer requires authorization for foreign nationals of Indian descent to purchase residential property. 100 percent foreign equity is permitted for the construction of power plants. Profits may be brought back home [7], [8].

4. Foreign investors are no longer required to sell their shareholdings at prices set by the Reserve Bank. Since September 15, 1992, it has been permitted on stock exchanges at market prices with authority to repatriate the profits.
5. On April 13, 1992, India ratified the Multilateral Investment Guarantee Agency Protocol to safeguard foreign investments.
6. Through an Ordinance dated January 9, 1993, provisions of the Foreign Exchange Regulation Act were liberalized, and as a consequence, businesses with more than 40% foreign stock are now given the same treatment as businesses with 100% Indian ownership.
7. As of May 14, 1992, foreign businesses are permitted to utilize their trademarks on domestic sales.
8. The Finance Ministry has agreed to permit 100 percent foreign partner participation in investment banking provided they contribute capital of at least US$100 million. Companies investing more than US$50 million will be given a 51 percent ownership in the joint venture, while those investing less than US$50 million would only be given a stake of less than 40%.

1995 SEBI Regulations

According to the rules, institutional foreign investors must register with SEBI and acquire a certificate from SEBI.

The applicant's track record, professional competence, financial soundness, expertise, and general reputation for fairness and honesty are all taken into consideration by SEBI while granting the certificate: If the applicant is an institution founded or incorporated outside of India as a pension fund, mutual fund, or investment trust, or an asset management company, nominee company, bank, or institutional portfolio manager, e.g., the applicant is such, the RBI will determine whether the applicant is subject to appropriate foreign regulatory authority, whether the applicant has been granted permission by RBI under Foreign Exchange Regulation Act for making investments in India as a foreign institutional investor, and whether the applicant has received the aforementioned permissions[9], [10].

Upon payment of the required payments, the certificate in FormBis issued. It is valid for 5 years and may be renewed at a later date. Additionally, provisions are given for the establishment of sub-accounts on whose behalf FII intends to invest in India. The number of shares purchased by any firm shall not exceed 10% of its entire issued capital. Foreign institutional investors' investments are likewise subject to GOI guidelines.

The appointment of a domestic custodian, designation of a designated bank, upkeep of correct books of accounts, records, and their preservation for five years, as well as communication with the Board or Reserve Bank of India, are among the general duties and responsibilities of FIIs. After a show-cause notice and investigation, defaults result in certificate suspension and revocation.

Relevance and Function of Foreign Investment

Historically, emerging nations depended on foreign direct investment to augment local savings, introduce new technology, skills, and goods, as well as to bring in foreign currency.

In our nation, it had remained mostly constant at about Rs. 110 crores until 1987, when the government made significant attempts to entice foreign money as a more advantageous option than borrowing with a promise of fast-track approval. When foreign investment reached Rs. 239 crores in 1988 and Rs. 316 crores in 1989, the effect was felt. Political instability caused foreign investment to decrease by 59 percent in 1990 from its peak in 1989. When compared to South Asian nations, our foreign investment and trade restrictions have led to an extremely low amount of foreign direct investment. A significant share of the resources needed for investment in the public and private sectors are raised from the capital market as part of the liberalization of the Indian economy and reliance on market forces. Savings flows will grow when the capital market's demand for capital rises, but only if the efficiency of the capital market's main and secondary components increases. They need to be more transparent, have a wider variety of risk-return combinations, and have better liquidity.It must also be acknowledged that a growing dependence on market mechanisms is the only way to accomplish technology transfer, export promotion, and access to foreign cash. The two mechanisms that link the local economy to global markets are trade and foreign investment. Trade and foreign direct investment obstacles may be decreased by relying more on market mechanisms.

An estimated $ 349 billion in total foreign direct investment was made in the world in 1996, of which $ 129 billion went to developing nations. The majority of foreign direct investments were made in wealthy nations. The majority of the $ 42 billion invested in China by Hong Kong-based companies, and the overall stock of foreign direct investment by the end of 1995 was $ 110 billion. United States ($712 billion), United Kingdom ($312 billion), Japan ($298 billion), and Germany ($428 billion) were the four largest industrial nations' respective shares.The flow of foreign investment is shown between the years 1991–1992 and 2001–2002. Foreign investment surged, beginning in 1993–1994 at $4.2 billion, continuing to $4.9 billion in 1994–1995 and $5.5 billion in 1996–1997. It totaled $4 billion from April through December 1996. The inflows were boosted by internal reasons such promising economic prospects, a favorable market return differential compared to industrial nations, and currency rate stability. The undervaluation of Indian stocks and, more recently, the Mauritius factor, which is a tax haven from which to invest, were the main external factors encouraging inflows into India. More than half of India's external financial requirements have been covered by inflows of foreign investment. Foreign investment inflows made a smart comeback in 1999–2000 after suffering a severe setback in the wake of the South East Asian crisis in 1998–1999. and the status was mostly maintained in 2000–01. The amount of total foreign investment, which includes direct and portfolio investments, declined precipitously to US $ 2.10 billion in 1998-1999 as a result of the Asian Crisis from an average of roughly US $ 5.39 billion for the four years ending in 1997-1995. They returned to health in 1999–2000, reaching US$ 5.18 billion, and the improvement was continued in 2000–2001, with a total inflow of US$ 5.10 billion. During the 1990s, FDI's source and direction mostly remained unaltered. During 2000–01, companies registered in Mauritius and the US were the major sources of foreign direct investment (FDI) into India, followed by Japan and Germany. The majority of FDI was increased into engineering industries, services, electronics and electrical equipment, chemical and associated goods, food and dairy products, computer hardware and software, and engineering industries.

DISCUSSION

Report of the Working Group on Non-Resident Indian Investment

A working group was established in October 1994 under the direction of Shri O.P. Sodhani, Executive Director of the Reserve Bank of India, to examine the various incentives and

schemes available to NRIs for investing in India as well as the procedures established for the purpose. The group's recommendations to the government for modification or amendment to the current scheme, policies, and procedures. In August 1995, the group presented their findings. The following are the Group's main recommendations.

The 40 percent plan on repatriation basis is recommended for elimination since it is obviously unlawful under SEBI regulations for NRIs to acquire a 40 percent ownership in a fresh offering. The areas/sectors open to NRIs under this plan should be combined with the 100 percent repatriation program, increasing rather than decreasing investment possibilities, to prevent diluting the options for NRIs to enter the market. Subject to the shares being valued in accordance with the valuation rules, the repatriable direct investment plan may also cover the sale of departing shares to NRIs or OCBs on a repatriation basis. Free reparability of capital and profit was advised for NRI and OCB investments in housing and real estate, coupled with the removal of the 3-year lock-in period and the 16% profit-remittance cap. It was suggested that the present limits, which call for a five-year lock-in term and eligibility requirements that the company's shares must have been trading at par for two years, be lifted in order to attract NRI investments under the sick unit's program. The 100% non-repatriation plan should be scrapped, the Group said. It was also advised that under the general license provided for NRI investment in different sectors, monies created from NRI deposits as well as accruals from prior non-repatriable investments be employed in the same way as funds of other residents.

The Group suggested parity between NRIs/OCBs and FIIs in terms of portfolio investment. The NRI/OCB individual maximum may be raised to 5%. Additionally, NRIs and OCBs may be permitted to purchase up to a maximum of 24 percent of the company's paid-up capital without a general body decision. In terms of capital gains tax, the Group also advocated for fiscal parity between NRIs/OCBs and FIIs. The Group advised the removal of all sectoral restrictions on NRI/OCB direct investment. This suggests that the agricultural and plantation sectors are now accessible to direct investment by NRIs, subject to local regulations.The Non-Resident Rupee Deposits Scheme gives banks the discretion to collect deposits, set interest rates, and use money for lending activities without adhering to priority sector lending guidelines. Banks have increased their interest rates on these deposits as a result. From the quarter that concluded in December 1994 forward, the tax-free interest received on the deposits is also now returnable. Continued use of this technique would result in a large loss of foreign currency due to increasing interest costs. As a result, the Group suggested ending this Scheme.

Budgetary Policy

There is surplus capacity and persistently high unemployment. The notion that government fiscal policy may be utilized in a counter-cyclical way to stabilize the economy was at the heart of the so-called Keynesian Revolution in economic policy making. Discretionary fiscal policy refers to planned adjustments to tax rates or government spending aimed at calming the economy. Once we know the intended direction of the change in GDP, it is usually simple to estimate the direction of the necessary adjustments in spending and taxes. This is because government expenditure stimulates aggregate demand while taxing reduces it. The timing, size, and combination of the changes, however, provide more challenging problems. A key instrument for achieving economic stability is fiscal policy. From about 1945 to roughly 1970, when fiscal policy was at its height, many economists held the belief that the economy could be properly stabilized by simply changing the quantity of the government's taxes and spending. That time has passed. The majority of economists today are aware of fiscal policy's many limits.

Discretionary fiscal policy's limitations

According to the discussion on the preceding few pages, increasing government spending and reducing taxes in some combination would be all that is necessary to get the economy back to full employment. Why do many economists think that these measures are just as likely to hurt as they are to help? The implementation of discretionary fiscal policy is everything from straightforward, which is part of the explanation.

Function of Independent Fiscal Policy

All of the aforementioned challenges point to the difficulty of using discretionary fiscal policy to tinker with the economy. The term "fine-tuning" refers to using monetary and fiscal policy to balance off almost all changes in private sector expenditure and maintain GDP at or very close to its potential level at all times. However, neither economics nor politics have developed enough to enable decision-makers to reverse the effects of each aggregate demand shock. However, many economists continue to contend that when a recessionary gap is significant enough and lasts long enough, gross-tuning may be necessary. Gross-tuning is the term for the sporadic employment of monetary and fiscal policy to close significant and enduring GDP disparities. Gross-tuning proponents contend that when a GDP gap is significant and has lasted for a considerable amount of time, fiscal policy may and should be employed to aid in the economy's restoration to full employment. Some economists hold the view that fiscal policy should never be employed to stabilize the economy. Instead, they would argue, tax and spending policies shouldn't be changed due to short-term concerns but rather should be the result of public decisions on the long-term size and funding of the public sector.

Monetary Commission

A Finance Commission must be established by the President in accordance with Article 280 of the Constitution in order to transfer non-Plan income streams. The Commissions' duties include making recommendations to the President about the allocation of the States' share of the net tax profits to be split between the Union and the States. the rules that should apply to any financial situation between the Union and the States, including the payment of grants-in-aid by the Union to the revenues of the States.

The creation of the Finance Commission is crucial because it makes it possible to modify the financial arrangements between the Center and the units in response to shifting needs and conditions. This clause has the enormous benefit of introducing flexibility into the connection.Since the Constitution's inception in 1951, the Government has so far constituted ten finance commissions. The recommendations of the Finance Commissions may be divided into three categories: grants-in-aid, loans from centers to States, and the division and distribution of income tax and other taxes.The Eighth Finance Commission, headed by Y.B., met for the first time. Chavan introduced a new formula for allocating the proceeds of the income tax among the States: 10% would continue to be distributed among the States based on income tax collection; 90% of the proceeds of the income tax would be distributed among the States based on the following criteria: 25% based on population; 25% based on the inverse of the state's per capita income multiplied by population; and 50% based on the basis of the state's per capita income.

This three-factor formula's main goal was to ensure that there was a high level of parity among the States. With a few minor adjustments, the Ninth Finance Commission mostly adhered to the methodology above. One additional requirement was introduced by the NFC. Using the 1981 census data, a composite index of state backwardness was created based on

the population of scheduled castes and scheduled tribes as well as the number of agricultural workers in each state. The NFC asserts that the composite rating would mostly represent a state's poverty and sluggishness. The states with a higher part of the two components must shoulder significant financial obligations. The following formula/criteria were introduced by the Tenth Finance Commission after it reviewed the formulas of the Eighth and Ninth Finance Commissions to determine the shares of the various States in the shareable proceeds of income tax: 20% based on population in 1971; 60% based on the distance of a State's per capita income from that of the State with the highest income; 5% based on area adjusted; and 5% based on the index of inequity.

Trading Protocol for the Stock Market

A trading floor is available at exchanges where securities are bought and sold. To have the ability to trade securities on the stock market, individuals or businesses (brokers) must pay for a seat or membership. The trading that occurs on the stock market floor resembles an auction since those wanting to sell a client's shares want to get the highest price, while those representing the buyer-clients want to get the lowest price. Members get bids or offers, as the case may be, from other members when they indicate their desire to purchase or sell a certain number of shares of a particular company. Sellers either hold shares until an acceptance bid is made or accept the highest offer. A member has the option to purchase or sell.The postings, where securities are exchanged, are only open to members. The "open outcry" provides a very straightforward way of trade-matching that has been used in commodities markets for millennia. By yelling out bid and offer price offers in the trading "pit," buyers and sellers are matched up immediately. The new screen-based exchanges now mirror the physical order matching mechanism. The computerized method is quickly gaining momentum in trading pits. Market-makers and corporations are the principal users of the new electronic media for carrying out significant transactions.

At the retail level as well, online trade platforms are becoming more and more popular. Electronic quotation systems that provide quick price quotes are used by the most advanced stock exchanges. Companies that want their prices published must adhere to strict guidelines on minimum capital, assets, and shareholder requirements. Specialists have stakes in certain stocks and are prepared to purchase or sell them. They are required to keep the securities entrusted to them in a fair and orderly market. For their customers, floor brokers trade stocks.

Market makers, who are prepared to purchase or sell a certain stock in response to consumers' requests sent over a telecommunications network, facilitate transactions. Market makers increase the liquidity of the stock market since they are obligated to build a market constantly in an attempt to keep prices stable. Market makers act as both brokers and investors, as opposed to exchange brokers who connect buyers and sellers. The bid/ask spread is the fee that market makers charge for the transactions they carry out. As a result, transaction costs increase.

The flow of buy and sell orders for each stock creates the market. By stating the name of the stock, whether to buy or sell it, the number of shares to be bought or sold, and whether the order is a market ordertransact at the best priceor a limit orderplace a limit on the price at which a stock may be bought or soldinvestors communicate their orders to brokers. Investors who place a limit order may be able to purchase a stock for less money, but there is no assurance that the price will eventually rise to the limit. For one day or longer, orders may be placed.

Investors who open a margin account with their broker may buy stocks on margin (with borrowed money). When they believe the price will fall, they may sell the stock short or short

the stock. In a sense, they are borrowing the stock from the investor when they sell it short and must return it to them. Earnings for short sellers are the difference between the price at which they first sold the stock and the company's purchase price. There is also the brokerage mechanism, which is used for diverse products in thin markets. For traders who often trade and have little immediate or liquidity needs, this is perfectly acceptable. Without adding things to their books, brokers utilize their contacts to discover buyers and sellers or are contacted by customers of other brokers. An auction might be scheduled in the worst-case scenario, if the procedure fails. tiny regional stockbrokers often trade the shares of tiny companies on a "matched bargains" basis. Matching techniques are used to create markets for stocks and choose the starting bids for auctions. Before the market begins, "limit orders" from clients are gathered.

These orders define the amount of the deal and an acceptable price range. The market clearing price is then established at the point when net demand is almost zero after these buy and sell orders have been combined. A market maker may execute these limit orders against his own inventory utilizing this whole demand/supply schedule as an offer curve. Dealers maintain liquidity in these markets in exchange for benefits they get from the stock exchange. The quote-driven mechanism and the order-driven mechanism are the two basic methods for obtaining liquidity. Dealers publish a "bid" price at which they are willing to purchase up to a certain maximum quantity and a "ask" (or offer) price at which they are willing to sell in quote-driven marketplaces. They then fulfill orders using their stock, altering pricing as necessary. Dealers (sometimes referred to as middlemen) continuously send limit orders to the stock exchange computer in order-driven markets. An instruction to purchase (or sell) shares up to a specific maximum at a price equal to (or higher than) the stated level is known as a limit order. These orders are "crossed" or, if feasible, executed against already-existing limit orders, but other than that, they are simply added to the order book, which serves as the market's price schedule. Clients may also submit limit orders.

They may also use the computer to place market orders, which are price-unconditional and instantly matched against the best limit order price. A person might place an order with a salesperson at a brokerage business if they wanted to purchase or sell a security. The order must include information such as the name of the security's issuer, the kind of security, whether it is for sale or buy, the size, type, price, and duration of the order's validity. Market, limit, short sell, and stop orders must be specified under type of order.On stock exchanges, order size trading is often done in round lots. For the majority of common stocks, 100 shares are regarded as one round lot. An odd lot is a quantity that is not equal to 100 shares. Both round and odd lots may be ordered. Odd lots often have greater transaction fees. There is no separate order size classification for securities other than common stock or common shares, however there may be a minimum order size.

The most typical order type submitted by an individual investor is a market order. An order to purchase (or sell) at the lowest (or highest) price presently being offered is referred to as a market order. The asking price or the buying price may not match. Consider a market purchase order first. The shares can fluctuate inside the bid-ask price while other investors concurrently place market orders to sell. Second, additional transactions that occurred before the order or new information that caused a change in the bid-ask spread might cause the bid-ask spread to shift between the time the order is made and the time it is executed. So, by utilizing a market order, an investor ensures execution with some price uncertainty.Purchase or sale orders with a minimum or maximum price are known as limit orders. Limit orders regulate the price received or paid, but the investor is unable to predict if or when the order will be honored. An investor who sees the price fluctuating within a range and seeks to sell or

purchase the stock at a favorable price within the range and is ready to take the risk of the order not being filled may use a limit order.

Investors in short sales may sell shares they do not already own. Short sales are the name given to this sort of transaction. The physical sale of a securities occurs when an investor shorts it. The brokerage business either loans the investor the security or borrows it from another investor since the investor does not own the security. The securities maintained by the brokerage company for other investors are often where the borrowed securities originate from. Investor-held securities are referred to as securities registered "in street name" when they are stored with a brokerage business. If the company does not already own the shares it wants to sell, it will borrow them from someone else, usually another broker. In most cases, the investor whose shares were borrowed and sold wouldn't be aware of the transaction, and they certainly wouldn't know who had borrowed the shares. Since the shares were physically sold, the corporation would pay the buyer of the shares rather than the investor whose shares were borrowed as dividends. The investor whose shares are borrowed must get the dividends in order for the short sale to not negatively impact him or her. In order for the individual whose shares were borrowed to receive any dividends received on the stock that was sold short, the person who sold the shares short is responsible for providing the necessary cash. The short seller replaces the borrowed shares by repurchasing the shares at a later date.

Only when the stock price hits or crosses a defined limit are stop orders executed. The stop price is the price at which the transaction is initiated. The order turns into a market order once a transaction occurs at the stop price. A stop loss order may be thought of as a conditional market order as a result. When other people make transactions that are equal to or greater than the stop price, a stop buy order becomes a market purchase. If the price of the shares rises further, the investor may issue a stop loss order with a higher stop price. The price at which the shares will actually trade, like with other market orders, is unclear since trading prices may change the stop price before the stop loss order can be carried out.Short sales often go hand in hand with stop purchase orders. Any price gain hurts the short seller since the share must be replaced after a short sale. The purpose of a stop purchase order is to restrict how much a short seller may lose.

For orders other than market orders, an investor must indicate how long an order will remain in effect. With a day order, the broker is directed to fulfil the order by the end of the business day. By the end of the day, if it is not full, it is automatically canceled. If the investor doesn't provide a timeframe, it is presumed that the order is for one day. The order must be fulfilled before the end of the week or month, otherwise it will be canceled. Orders that are good until cancelled are still in effect unless the investor expressly cancels them. The broker is given the option of filling the order right now or killing it. Spot transactions must be settled by delivery and payment either on the contract date or the following day. A clearing house makes it easier for members to pay one another, distribute securities, and settle contracts.

The over-the-counter (OTC) market is where stocks that are not listed on organized exchanges are exchanged. The OTC market permits secondary market transactions much like the organized exchanges, although it lacks a trading floor. Instead, a telecommunications network is used to fulfill purchase and sell orders. There is no need to purchase a seat to trade on this exchange since there isn't a trading floor, however registering with it is required.

Trading on Margin

When investors trade on margin, they borrow a portion of the stock's purchase price from their brokers, leaving the acquired shares with the brokerage business in street name since the securities are used as security for the loan. Typically, the margin credit interest rate charged

by the broker is 1.5% more than the rate paid by the bank providing the loan. In terms of transaction volume, NSE (National Stock market) is the biggest stock market in India and the third largest in the world. Several of India's top banks, insurance corporations, and other financial intermediaries jointly hold the NSE (National Stock Exchange), although ownership and operation are independent businesses. In India's capital and financial markets' modernization, the NSE has continued to play a key role. In order to do this, the NSE (National Stock Exchange) established the NSCCL (National Securities Clearing Corporation Ltd.), the country's first clearing corporation. The NSCCL was a turning point in India's spot equities market (and subsequently, derivatives market) trading by offering novation.

The National Securities Clearing Corporation Ltd. (NSCCL), a fully owned subsidiary of the National Stock Exchange (NSE), is a member of the NSE group. It was formed in August 1995, and in April 1996 it began carrying out clearing activities. It was established to encourage short, regular settlement cycles, give a counter-party risk guarantee, run a strict risk containment system, and increase public trust in clearing and settlement of securities.

Settlement and Clearing

The National Securities Clearing Corporation Limited (NSCCL) manages component SGL for settling transactions in government securities as well as the clearing and settlement of deals completed in the CM section of the NSE (National Stock Exchange).

Clearing Between Regions

Inter-region clearing is facilitated by the NSCCL (National Securities Clearing Corporation Limited). It features a Central Clearing Center in Mumbai, as well as Regional Clearing Centers in Delhi, Kolkata, and Chennai. At a clearing center of their choice, members have the option of delivering or receiving the securities.

Handling of Certificates

The National Securities Clearing Corporation Limited (NSCCL) moves securities in the regular pay-in and pay-out on behalf of the clearing members from and to Regional Clearing Centers (RCC) and the Central Clearing Centre (CCC) at Mumbai in order to provide a level playing field to members regardless of their location.

Pre-delivery Checking

Pre-delivery verification was originally used by the NSCCL (National Securities Clearing Corporation Limited) to identify fraudulent documents, such as phony or forged certificates or lost or stolen share certificates.

Settlement Without Materials

The issue of fake/forged and stolen shares could only be solved by dematerialised trade and settlement. The percentage of shares released in the dematerialized form by the NSCCL (National Securities Clearing Corporation Limited) has grown as a result of SEBI mandating demat settlements for an ever-increasing number of securities in a staggered way.

Management of Risk

Risk mitigation techniques have also been implemented into the NSCCL. A risk group created by the NSCCL (National assets Clearing Corporation Limited) increased surveillance of members' positions with a concentration on certain high-risk assets that are volatile and attract significant volumes.

Along with providing the option for early pay-in of securities in demat mode, a structured exercise that requires members with abnormally large pay-in liabilities to make advance pay-ins of money has also been implemented.

Borrowing or Lending of Securities

The National Securities Clearing Corporation Limited (NSCCL) offers a capacity to lend/borrow securities/funds at market-determined rates via its automated lending and borrowing mechanism. This makes it easier to provide securities on time, which boosts the system's effectiveness.

Membership in Professional Clearing

The Stock Holding Clearing Corporation Ltd. was accepted as the first professional clearing member on the CM Segment by the NSCCL (National Securities Clearing Corporation Limited), which launched the professional clearing membership program.

Settlement of Derivatives

In addition to clearing and settlement services, the NSCCL (National Securities Clearing Corporation Limited) also offers risk management for the derivatives market.

Different Depositories

It has also been made possible to clear and settle securities in dematerialized form via the Central Depositories Securities Limited (CDSL), which has been linked to the National Securities Clearing Corporation Limited (NSCCL). You knew? The National Securities Clearing Corporation Limited, often known as NSCCL, accepts and holds FDRs issued in its favor. Members now get enhanced services since they are no longer needed to pay custodial fees and instead may receive immediate credit and benefits.

CONCLUSION

In conclusion, the linked global economy is largely shaped by foreign direct investment. While opening up possibilities for technology development, information sharing, and economic progress, it also necessitates careful evaluation of any possible drawbacks. In order to promote ethical investing practices, policymakers must simultaneously put in place efficient protections. Stakeholders may negotiate FDI's difficulties and optimize their contributions to shared prosperity and sustainable economic growth by acknowledging the diverse nature of FDI. Policymakers may create tailored policies that attract profitable FDI, maximize its advantages, and minimize possible hazards by recognizing the intricacies and ramifications of FDI. Businesses and investors may use FDI to open up new markets, promote innovation, and increase their competitiveness globally.

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CHAPTER 24

DIFFERENT TYPES OF DEPOSITORIES AND CUSTODIANS

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ABSTRACT:

Depositories and custodians play essential roles in the modern financial ecosystem, providing safekeeping, settlement, and servicing of financial assets for investors, institutions, and market intermediaries. This paper explores the significance and functions of depositories and custodians, examining their roles in facilitating securities trading, enhancing market efficiency, and ensuring investor protection. It delves into the different types of depositories and custodians, including central depositories, global custodians, and local custodians, and the services they offer. The study also analyzes the challenges and opportunities faced by depositories and custodians in the context of evolving financial markets and regulatory frameworks. Understanding depositories and custodians is essential for investors, financial institutions, regulators, and policymakers, as it enables informed decision-making and supports the smooth functioning of securities markets.

KEYWORDS:

Central Depository, Clearing, Custodians, Dematerialization, Depositories, Depository Participants (DPs).

INTRODUCTION

Due to the phenomenal growth of India's primary and secondary securities markets as well as the entry of large traders from both domestic and international financial institutions, many flaws and inadequacies in the market infrastructure have come to light[1], [2]. Trading, clearing, settlement, transfers, registration, and record keeping using the current manual techniques have been shown to be laborious and time-consuming. Additionally, this decreased system efficiency and raised systemic hazards[3], [4].The risk elements associated with counter party risk, credit risk, faulty deliveries, lengthy delivery delays, fake scripts, forged certificates, incorrect signatures, and slow and theft of shares have all significantly increased as a result of the stock trading industry's expansion.

All of this finally resulted in the introduction of a brand-new, contemporary infrastructure that includes depositories, paperless trading, and computerized transaction recording. Establishing Stock Holding Corporation of India Limited (SHCIL), in which ICICI, IDBI, IFCI, RBI, UTI, and LIC invested collectively, was the first step in this process. The establishment of depositories has been a significant change in the Indian capital market[5], [6]. The goal of a depository is to allow scrip-less trading on stock exchanges and maintain ownership records of securities in an electronic book entry format, therefore lowering settlement risk. The Finance Ministry ordered the development of the National Clearance and Depository System, which the Government issued Ordinance for Depositories in 1995, to further improve the depository and custodial services.Two depositories, National Securities Depository Limited (NSDL) and Central Depository Services (India) Limited, have been registered under the Depository Act of 1996 by SEBI.

The primary strategic goals of NCDS are to:

1. Free the securities business from the paper work bottleneck;

2. Lower the cost of processing paper;
3. Eliminate transfer delays; and
4. To lower systemic hazards.

Dematerialization of new and existing issues, execution of book entry transfer of ownership of securities, implementation of delivery versus payment system, provision of both operational and transactional facilities and scrip hypothecation, and implementation of beneficial owner record keeping are specific, crucial, and technical objectives to achieve the overall objectives.The following securities may be maintained in a depository in a dematerialized form:

1. Shares, bonds, debentures, or other marketable securities of a similar type issued by any corporation or other legal entity.
2. Mutual fund shares, stakes in venture capital funds, rights to collective investment plans, commercial paper, certificates of deposit, debt that has been resold as securities, money market instruments, government bonds, and other unlisted securities.

All of its participants, issuers' agents, clearing houses, clearing companies, stock exchanges, and other depositories must be in constant electronic contact with the depository.The depository must demonstrate to SEBI that it has measures in place to safeguard the interests of those purchasing and selling securities held by the depository. Only after being satisfied that payment has been paid, the depository must record the transfer of the security in the name of the transferee.

Every depository is required to keep track of all dematerialized and rematerialized securities, including the identities of the transferor and transferee and the dates on which the securities were transferred. There should be a registration of beneficial owners, an index of them, as well as data of their stock holdings as of the end of each day. Other records of approval, notice entry, and cancellation of pledge or hypothecation, participant information, information on securities determined eligible for dematerialization in the depository, and other paperwork required for carrying out the depository's duties must be maintained. Every depository is required to inform SEBI of where the records and papers are kept. Records and papers must be kept by the repository for at least five years.Every depository is required to provide all necessary assistance for the efficient, accurate, and timely clearance and settlement of securities transactions as well as the conduct of business to beneficial owners, issuers, issuer's agents, custodians of securities, other depositories, and clearing organizations. When a depository or participant offers such advice, they must disclose the interests of any dependent family members and the employer, including whether they have a long or short position in the underlying securities.

A Depository, Depository Participants, Company/Registrars, and Investors all take part in the activities of the Depository System. The business is sometimes referred to as the Issuer. A depository (NSDL and CDSL) is a business similar to a central bank, or reserve bank, where an investor's assets are stored electronically by depository participants. The method through which shares are kept in electronic form and are the agent of the Depository is known as a Depository Participant. Additionally, they act as the investor's representatives, serving as the Depository's conduit between the investor and the firm. The Depository system acts quite similarly to the banking system, to use an example. A bank keeps money in accounts, whereas a depository keeps securities for its customers in accounts. A bank moves money from one account to another, while a depository moves securities.

Both approaches allow for the transfer of assets without actually touching the money or securities. Banks and the Depository are both responsible for the security of money and securities, respectively. The business must install the required hardware and software and establish an agreement with NSDL/CDSL (the depositories).

Investor Depository Services

As a Depository Participant with the Central Depository Services (India) Limited (CDSL) and the National Securities Depository Limited (NSDL). In India, a depository system connects issuers, national level depositories, depository participants, and clearing houses/stock exchange clearing corporations. Our demat services company is unique in that all of its activities are ISO 9001: 2000 accredited and equipped with cutting-edge technology and operational skills. Our demat services have evolved over time, and we now provide our customers internet access to account statements and transaction notifications through SMS. Without the bother of managing paper-based transcripts, demat services provide a safe, practical, and paperless method to manage investments in shares and other security instruments over time[7], [8].

Dematerialization, or "Demat," refers to the conversion of an existing physical share certificate to an electronic counterpart for the same number of holdings. The extensive and laborious paper work required in the scrip-based system is abolished, which is a direct result of the significant advance achieved in the field of information technology. Modern technology makes it possible for share transactions and transfers to be performed without the need of share certificates or transfer deeds. This is done once the share certificates have been transformed from physical to electronic form. Dematmakes an effort to avoid the lengthy and difficult procedure of transferring shares in the name of purchasers, as well as its inherent issues with poor deliveries, processing delays, fraudulent postal interceptions, etc. An investor may still own shares in physical form; dematerialization of shares is optional. If the person wants to sell the shares via stock exchanges, they must first demat them. In a similar vein, if an investor buys shares, they will be sent to them in demat form[9], [10].

To govern things connected to and incidental to the operation of depositories and demat activities, the Depositories Act, 1996, was adopted. National Securities Depository Limited (NSDL) and Central Depository Services Limited (CDSL) are the two depositories that are currently in operation. A Depository, Depository Participants, Company/Registrars, and Investors all take part in the activities of the Depository System. The business is sometimes referred to as the Issuer. The company/registrar (known as Benpos) will get the list of demat account holders and the number of shares they have in electronic format on the Record Date from the Depositories (NSDL/CDSL). The corporation in question will offer payout warrants to the owners of demat accounts based on Benpos. Shareholders who hold their shares in demat form have the same rights as those who own them in physical form. Therefore, as a shareholder, you will be entitled to receive the Annual Report and have the right to attend the AGM. To receive a distinct Client ID number, one must first register an account with a Depository Participant (DP).

After that, one must submit the physical shares they want to dematerialize together with a completed Dematerialization Request Form (DRF) to the DP. Upon receiving the shares and the DRF, the DP will electronically seek confirmation of demat from the Company/Registrars through the Depository. There will be a distinct transaction number for each request. Along with a covering letter asking the Company/Registrars to confirm the demat, the DP will concurrently deliver the DRF and the shares to them. The Company/Registrars shall confirm demat to the Depository after they have completed any required document verification on

those they have received from the DP and deemed to be in order. The DP, who is in charge of holding the account, will be given this confirmation by the Depository. The DP will credit the account with the shares that have been thus dematerialized after it receives this confirmation from the Depository. Following that, the DP will hold the shares in dematerialized form on your behalf. Moreover, you will come to hold these dematerialized shares in a favorable manner.

DISCUSSION

Stock Exchange

Any organization or person, whether incorporated or not, created with the intention of aiding, regulating, or overseeing the business of buying, selling, or dealing in securities is referred to as a stock exchange.

Activities of the Stock Exchange

1. The stock market offers listed firms' liquidity.
2. It provides quotes to the listed firms, which facilitate trade and enable the market generate money.
3. Companies were able to acquire more money by gaining the listing and trading capabilities, which encouraged public investment.

In India, there are 22 stock exchanges. Among the various stock exchanges, the important ones include those in Ahmedabad, Delhi, Kolkata, Chennai, and Bangalore. These stock exchanges are served by 3,000 brokers and 20,000 sub-brokers.

The expansion of world stock exchanges

1. Demat-based trading
2. Trading done electronically
3. Online shopping

Screen-based trading has been offered by the NSE, BSE, and OTCEI. By June 30, 1996, all other exchanges (apart from those in Guwahati, Magadh, and Bhubaneshwar) are required to implement computerization and screen-based trading. This will increase investor transparency, decrease spreads, make it possible to monitor prices and volume more effectively, and speed up settlements.

Bombay Stock Exchange

The Native Share and Stock Brokers Association, also known as "BSE," the Mumbai stock market, was founded in 1875. Even older than the Tokyo Stock Exchange, which was founded in 1878, it is the oldest in Asia. It is a voluntarily organized, nonprofit Association of Persons (AOP) that is in the process of becoming a demutualized corporate company.

It was the first stock exchange in the nation to get official registration from the Indian government in 1956 as a result of the Securities Contracts (Regulation) Act. The exchange promotes the interests of investors and guarantees that their complaints, whether directed at the firms or its own member brokers, are resolved while offering an effective and transparent market for trading in securities, debt, and derivatives. By conducting investor education programs and making accessible the essential information inputs, it also works to educate and inform investors.Mumbai is the biggest of the country's 22 stock exchanges, with more than 6,000 companies listed. More than two thirds of the country's total volume is accounted for by the BSE. The BSE'sensex' is a popular market index for the BSE.

Indian National Stock Exchange (NSE)

The report of the high-powered research committee on the creation of new stock exchanges, which advised financial institutions promote a National Stock Exchange to provide investors from all across the nation access to the market on an equal basis, is where the NSE of India Limited got its start. Leading financial institutions supported NSE in accordance with the guidelines. Unlike other stock exchanges in the nation, the Government of India established NSE in November 1992 as a tax-paying Company. In June 1994, the NSE started operating in the Wholesale Debt Market (WDM) sector after being recognized as a stock exchange under the Securities Contract Act of 1956 in April 1993. Currently, 200 big firms are traded on the NSE; as the exchange stabilizers, this number is anticipated to further grow. A computerized market for debt and equity products is called the NSE. In order to promote stock exchange reform via system modernization and competition, the NSE, based in Bombay, was established in 1993. The National Securities Clearing Corporation (NSCC), a subsidiary of NSE, was established to enhance the settlement system and reduce the risks involved in it.

Primary Market

The primary market is where new securities are issued to generate money for investments or to pay off debts. Either via public concerns, rights issues, or offers for sale, they do this. If anybody and everyone may subscribe for the securities, it is a public issue. If the offer is solely extended to current shareholders, it is a rights issue. However, a private problem is one that is made available to a small group of individuals alone. Companies in the public and private sectors raise concerns that are public. In contrast to many other nations where issues are privately issued, around 130 issues occur each month in India. These issues are actively advertised to individual investors throughout the nation.By purchasing or selling securities on the secondary market, an investor may modify his holdings of assets in response to changes in risk and return assessments. He may use it to satisfy his liquidity demands by selling assets for cash. It consists mostly of stock exchanges, which act as a trading platform for equities. Under the control of the exchanges and SEBI's supervision, the securities are traded, cleared, and settled in accordance with a thorough, well-established regulatory framework. Only a registered broker may provide the investor with access to an exchange's trading platform.Depository System Since 1996, the Indian stock markets have undergone a significant transformation with the implementation of the depository system and scrip-less trading mechanism. This physical transfer of securities-based trading mechanism worked against the markets' ability to operate effectively, especially when substantial numbers of foreign institutional investors (FIIs) entered the market.

Participant Depository (DP)

The DPs provide the investors their services. Through these, the depository communicates with its investors as agents or participants. An investor needed to create an account with a DP in order to use a depository's services.

CDSL

The Mumbai Stock Exchange (BSE) has pushed CDSL as the secondary repository in India for trading in securities in electronic form, in collaboration with Bank of India, Bank of Baroda, State Bank of India, and HDFC Bank.

1. The primary goal of CDSL is to accelerate the development of scrip-less trading.
2. To provide the involvement of private investors in the depository a strong push.

3. To establish a competitive atmosphere that will be sensitive to the needs and interests of the user.

Increase Liquidity

Dematerialization of current scripts, dematerialization of new problems, dependable and effective settlement, re-materialization, and corporate actions (cash and non-monetary) are all services that the CDSL provides to the beneficial owner.The securities that the depositories hold is all fungible and stored in demat. While the depositories appear as registered owners in the company's records, the investors in securities appear as beneficial owners in the depository's records. However, beneficial owners are the only people who have rights in relation to securities. Having securities in demat form enables investors to transfer securities immediately in the event of purchases. The investor may avoid hazards connected with physical certificates, such as faulty delivery and fake securities, by not paying stamp duty on the transfer of assets. Through its representatives, known as Depository Participants (DP), a depository communicates with the investor. To use the services provided by a depository, a DP account must be opened with them. This is comparable to establishing an account at any bank branch to use the bank's services.

Guidelines for SEBI Issue Management

The share capital in the main market is included in book building and issue management by means of:

First Public Offering

Initial Public Offering (IPO) refers to a company's invitation to the public to subscribe to the securities issued via a prospectus; offer for sale denotes a company's existing shareholders' offer to the public to subscribe to their stocks through an offer document.

Norms for Issue Procedure Eligibility: businesses that issue securities using offer documents.

1. The prospectus in the event of a public offering or scale offer.
2. Offer letter in the event of a rights problem. both at the time of submitting the final offer document to the authorized stock exchanges and the registrar of businesses, as well as when the draft offer document is submitted to SEBI.

Pricing Problems

1. Through a public or rights issuance, a listed corporation may freely price equity shares and convertible securities.
2. Unlisted businesses that are permitted to offer securities to the public and who want to have their securities listed on a reputable stock exchange may also freely price their shares and convertible securities.
3. Compliance with the disclosure standards as set out by the SEBI from time to time is a requirement for an infrastructure company's free pricing of equity shares.
4. The Reserve Bank of India (RBI) must provide its consent before any bank may freely price their first public offering of shares or convertibles.

Contributions from Promoters and Lock-in Requirements

Promoters' contributions to various topics include:

1. The promoters of public offerings by unlisted firms shall provide at least 20% of the post-issue capital.

2. When unlisted firms make a scale offer, the promoters' post-issue capital must be at least 20%.
3. The promoters of public offerings by listed businesses shall provide guarantees equal to 20% of the planned issue or 20% of the post-issue capital.
4. For a period of three years, the minimum needed payment would be locked in.
5. Excess promoter contributions made in the event of a public offering by an unlisted firm would be locked-in for a year.
6. The last-issued securities will be locked in first.

Book Creation

A process known as "book building" is used to gather demand for securities that a body corporate plans to issue. The price of these securities is added to the notice, circular, or advertisement to determine how many of these securities will be issued. In an initial public offering (IPO), book building is essentially a procedure utilized for effective price discovery. It is a technique where investor bids are gathered at different prices that are higher than or equal to the floor price throughout the time that the IPO is open for business. After the bid closing date, the offer price is established. According to SEBI regulations, a firm issuing securities may do it in one of the following ways:

1. Through the book building process, the public will get 100% of the net offer.
2. 25% at the price established by book building and 75% of the net offer to the public through book building.
3. After the Book Built position during the issue price is established, the Fixed price position is handled as a typical public issue.
4. Time capital must be over 4.25 crores in order to begin the 100% Book construction procedure.
5. A book runner, often a chief merchant banker, is assigned for the 100% book construction process.
6. The prospectus should be written by the merchant banker, including with all disclosures (other than the price and quantity of shares), and filed with SEBI.
7. The board has the right to recommend changes to the draft prospectus to the merchant banker within 21 days of receiving it.
8. The merchant banker must request bids from potential customers or underwriters.

Agents for Share Transfers and Registrar to Issue

A registrar and transfer agent are a business entity in charge of performing the following tasks and maintaining a tangible record of a company's shareholders:

1. Managing share certificate transactions.
2. Managing business dealings including acts.
3. Managing share transfers and related transactions.
4. Managing investor and corporate interactions and communications.

CONCLUSION

In conclusion, the contemporary financial system is anchored by depositories and custodians, who provide crucial services that support investment and trading in securities. Depositories increase the efficiency of the market and investor trust by centralizing and safeguarding the holding of securities. In turn, custodians are crucial in protecting investment funds and offering institutional customers professional services. Depositories and custodians must adapt

as the regulatory and technological environments change in order to be at the forefront of the financial market infrastructure.

Stakeholders may use depository and custody services to successfully traverse the intricacies of the financial environment, optimize investment possibilities, and guarantee the integrity of international financial markets by comprehending their relevance and remaining informed of market changes. For investors, selecting trustworthy depositories and custodians is essential to protecting their assets and ensuring efficient portfolio administration.

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CHAPTER 25

MONITORING AND AUDIT OF CUSTODIANS BY SEBI

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ABSTRACT:

The monitoring and audit of custodians by the Securities and Exchange Board of India (SEBI) play a pivotal role in upholding investor protection, market integrity, and the overall stability of the financial system. This paper explores the significance and objectives of SEBI's monitoring and audit of custodians, delving into the regulatory framework and guidelines set forth by SEBI to ensure the safekeeping and efficient servicing of investor assets. It analyzes the responsibilities and obligations of custodians in compliance with regulatory requirements, risk management practices, and transparency in their operations. The study also evaluates SEBI's role in conducting regular audits, inspections, and risk assessments to enhance investor confidence and maintain market trust in custodial services. Understanding SEBI's monitoring and audit of custodians is essential for investors, custodians, financial institutions, and regulators, as it enables informed decision-making and reinforces the stability and credibility of the Indian financial market.

KEYWORDS:

Audit, Custodians, Custodial Services, Due Diligence, Monitoring, Regulations.

INTRODUCTION

Investors

1. Qualifies Institutional Investors:

Public financial institutions as defined by Section 4A of the Companies Act, FIIs, scheduled commercial banks, mutual funds, multilateral and bilateral development financial institutions, venture capital funds registered with the SEBI, foreign venture capital investors registered with the SEBI, state industrial development corporations, insurance companies registered with the Insurance Regulatory and Development Authority, provident funds with a minimum corpus of "25 crores," and pension funds are just a few examples of the types of institutions that fall under this category. The percentage of the Net Issue that is available for allocation is 60%. Mutual funds participating in the 5% reserve in the QIB section will also be eligible for allocation in the remaining QIB portion. 5% shall be available for allocation. QIBs will have access to the mutual fund reservation's unsubscribed component, if any. For QIBs, the minimum bid amount is more than $1,000,000 and increases from there. The highest offer cannot exceed the Issue, subject to any rules that may apply to the bidder. 10% of the bid amount in relation to bids put by QIB bidders on bidding is the Margin amount that applies to QIB bidders at the time that the bid cum application form is submitted[1], [2].

2. Non-Institutional Investors:

This group includes non-resident Indians, resident Indians, HUFs (under the name of karta), corporations, societies, and other legal entities.The 10% of the Net Issue that is eligible for allocation is Issue Size.Both QIBs and Retail Individual Bidders will be eligible to get the fraction of this category that has not yet been subscribed[3], [4]. If it is oversubscribed, a proportional distribution will be made. Maximum bid size not to exceed the size of the issue

subject to regulators as applicable to the bidder. Minimum bid amount for NIB's surpasses 1,00,000 and in multiple thereafter. Amount that Non-Institutional Bidders Must Pay When Submitting a Bid Cum Application Form To be paid in full at the time of bidding[5], [6].

3. Retail Individual Investors:

Individuals applying for equity shares with a bid sum per retail individual bidder that is less than $100,000 (including HUFs bidding in the name of karta). There is at least 30% of the Net Issue that can be allocated. This category's unsold inventory will be distributed to qualified institutional bidders and non-institutional bidders. In the event of an oversubscription, there will be a proportional distribution[7], [8]. For RIBs, the minimum bid is expressed as a number of equity shares. The highest offer should not be more than $1,000,000. Depending on the mode of payment, Retail Individual Bidders must pay the appropriate amount at the time their Bid Cum Application is submitted.Additionally, reservations may be made for:

(i) The issues'/promoter firms' employees and directors.

(ii) The issuer/promoter firms' current shareholders.

Price Range and Offset Price

The price range for the auction is disclosed to the investors. The floor price and cap price represent the lowest and higher ends of the pricing range, respectively. The pricing range's cap price should not exceed 20% of the floor price. The investor has the option to bid at any price within the price range (including the floor price and ceiling price). While the bid is open, the issuer, in collaboration with the BRLM (Book Running Lead Manager), may change the price band (upward or downward), as long as the bid remains open for at least three days following the modification. Retail individuals are permitted to bid at the "cut-off" price. Then, regardless of the issue price that is ultimately set via the price discovery process, they become eligible to be considered for allocation without needing the price as the particular number. They are required to pay the margin sum determined at the ceiling price. The other types of investors are not permitted to submit applications at the cutoff price[9], [10].

Nomination Center

A fully completed and signed nomination form must be submitted. The nomination form must be signed by all shareholders, including joint holders, if more than one individual hold shares. A registration number will be assigned to the nominee when the firm receives the form and verifies that it is complete. The nomination form that was provided by the shareholder will then be duplicated and returned together with an endorsement that includes the registration number and date. Only shares held in tangible form are eligible for nomination. Your nomination must be filed with your Depository Participant if the shares are demitted. Each folio may only get one nomination. Separate nominations are necessary for folios with various combinations of names of shareholders or names in a different sequence. The nominee has the right to request that the shares be transferred in his favor once a shareholder passes away. He or she must provide a written notification to that effect together with the share certificates of the shareholders who have passed away. The nominee may also give the shares the dead shareholder owned to a third party. If a nominee chooses to register shares in his or her name, he or she must provide identification documentation, such as a copy of a passport, driver's license, voter identification card, or other documentation that satisfies the firm. Along with a transfer request, the candidate should also provide a specimen of his

legally certified signature. Shares will be transferred in his favor and share certificates will be delivered to him with the proper endorsements once the nominee's papers are examined. The surviving shareholders must submit a request letter together with an authenticated copy of the deceased shareholder's death certificate and the relevant share certificates. When the firm receives the aforementioned papers, the name of the dead shareholder will be removed from its records, and the share certificates will be returned to the applicant/registered holder with the appropriate endorsement.

Factors Affecting the Demat System's Success

1. Concerns with technology and internet service providers for the expansion of electronic trading. The cost-effective transaction fulfillment should be provided at a single place via a genuine Internet trading system. It is wise and necessary for a broker or intermediary to provide customers with a complete solution at a single location in a net-based economy. Offering interfaces with banks, depositories, information feeds, and transaction completion efficiency are all examples of whole solutions. As a result, the service providers go beyond the simple order execution stage and become information providers.
2. Bandwidth optimization: Due to the restricted availability of adequate bandwidth in India, application software makes use of cutting-edge technology to maximize the available bandwidth.
3. The trading system's robustness and scalability the fact that the internet is a global platform that allows simultaneous access to an endless number of users at a given moment in time distinguishes it fundamentally from the traditional closed user group network used for transactions. Due to the need of having a proven capacity for scalability and resilience, which provides the ability to receive and process requests from numerous users at any one moment in time, every net-based program must now meet these requirements.

Custodians

While not trading members, custodians are clearing members. They settle deals performed by other trading members on behalf of their customers. A trading member may designate a custodian as the settlement agent for a certain deal. The custodian must state whether or not he intends to settle that deal. NSCCL allocates the obligation to the custodian if the custodian approves the transaction. The obligation is handed back to the trading member if the custodian rejects the deal.Custodians To get a Custodian Participant (CP) code from Clearing Corporation for the customers they intend to clear and settle for, clearing members must submit a request. Depending on the client's category, the request must be made together with the necessary papers, such as a SEBI registration number, a PAN number, etc.

Registration

The SEBI must have the custodians of securities registered. Before granting registration, the SEBI would consider all matters relevant to the activities of a custodian of services with particular reference to – whether the applicant: Fulfils the requirement of net worth (paid-up capital plus free reserves) of ` 50 crore; Has the necessary infrastructure including adequate office space, vaults for the safe custody of securities and computer systems capability required to effectively discharge his activities as a custodian;Has the requisite approvals to provide custodial services in respect of gold/gold-related instruments of mutual funds; or title deeds of a real estate asset held by a real estate mutual fund;Has in employment adequate and competent persons who have the experience capacity and ability to manage the business of a custodian; Has prepared a complete manual, setting out the systems procedures to be

followed by him for the effective/efficient discharge of his functions and an arms' length relationship to be maintained with his other business(es);Is not a person who has been refused registration by the SEBI/whose registration has been cancelled by the SEBI;His director/principal officer/any of his employees is involved in litigation connected with the securities market or has at any time been convicted of an offence involving moral turpitude/economic offence;The registration is in the interest of investor; andThe applicant is a fit and proper person.

The SEBI will consider the standards outlined in the SEBI Intermediaries Regulation, 2008 while deciding whether an applicant/custodian of securities is a suitable and proper person. The applicant has to be a corporation. A registration fee of £15,000 must be paid. Each three years, the registration would need to be renewed. The registration of a custodian is subject to a number of requirements. Additionally, it must carry out its duties in accordance with the SEBI Act and Regulations.

Additionally, the SEBI shall be notified in writing if any information provided to it is discovered to be inaccurate or misleading in any way or if it changes. The provision of custodial services with regard to securities, gold/gold-related instruments, or title deeds of a real estate asset owned by a real estate asset mutual fund may be restricted by the SEBI under the certificate of registration.

Code of behavior

The greatest level of professionalism, fairness, and honesty should always be maintained by securities custodians while performing their responsibilities.

1. Be quick in disbursing dividends, interest, and any other accruals of income on the securities kept in custody that he has received or collected on behalf of his customers.
2. Be continually accountable for the influx and egress of securities from custody accounts, the deposits and withdrawals of money from clients' accounts, and the provision of a full audit trail upon request from clients or SEBI.
3. Establish and maintain sufficient infrastructure to provide custodial services that satisfy customers, and the operational methods and systems should be well-documented and supported by operation manuals.
4. Maintain the client's privacy with regard to his affairs.
5. Take steps to guarantee that records are kept electronically, that continuity in record keeping is not lost or destroyed, and that there is a sufficient amount of backup of the records.
6. Create and keep securities records in a way that makes it easier to trace securities and get duplicate papers in the event that original records are lost for any reason.
7. Provide any assistance required for doing business in the areas of inter-custodial settlements and the transfer of securities and money to other custodial entities, depositories, and clearing organizations. Assure a fair and impartial connection with other companies, both in terms of personnel and infrastructure. Apply due diligence while managing and safeguarding the assets that you are in charge of.
8. Officers and workers performing custodial duties shall refrain from engaging in any other activities.

Agreement with clients and separate custody account: The custodian should form a separate custody account for each client, and the assets of one client shouldn't be combined with those of another. Each client should sign a contract with the custodian outlining the conditions under which he will take or release securities, money, assets, and documents from the custody

account, as well as obtain rights or entitlements on the client's securities. Additionally, it should clarify the custodian's obligation to offer insurance as well as the conditions and methods of each client's securities registration.

Maintaining records

The custodians should keep track of all of the following information on behalf of and for each client: securities, assets/documents received/released, money received/released, rights/entitlements resulting from securities held, registration of securities ledger, instructions received from/given to clients, and all reports submitted to the SEBI. These documents must be kept for at least five years, and the SEBI must be informed of the location of their storage. Every custodian of securities shall employ a compliance officer to oversee compliance with the SEBI Act, rules, notices, guidelines, instructions, and other directives issued by the SEBI or government, as well as to address investor complaints. Any non-compliance he notices must be reported to the SEBI promptly and independently. Information to SEBI: The SEBI has the right to request any information at any time on any aspect of a custodian's activity. Such information should be submitted within such reasonable time as may be specified by the SEBI.

DISCUSSION

SEBI's Norms and Practices for Custodians

For the custodians of securities to follow while interacting with other market players, the SEBI has established certain consistent rules and procedures. They must:

1. Function as a crucial component of the system. No custodian should, therefore, have any standards or procedures that would force them to operate independently from the clearing and settlement processes.
2. Join the clearing corporations/houses of the stock exchange(s) and take part in the clearing and settlement of all securities via them.
3. Abide by the appropriate stock exchange regulations in the exchanges where they have joined the clearing house or clearing organization. Client operations would be made easier, and client service fees would be decreased as a consequence.
4. Discuss with all of their customers the option of settling transactions via a clearing house or clearing corporation, highlighting benefits such

i. Time-bound correction of objections,
ii. No shortages,
iii. Risk reduction, and
iv. Cost effectiveness.

5. Emphasize that the associated advantages would not apply to "DVP trades" (i.e., Delivery vs. Payment transactions) if delivery of securities is not received or granted by the custodian via the clearing house/clearing company.
6. Adopt the consistent good/bad delivery rules, including the requirements for the Bad Delivery Cell to correct faulty deliveries, as set out by the SEBI and distributed to all stock exchanges, as revised from time to time.
7. Adopt the following standards in circumstances of transactions (DVP trades) when the custodian does not accept or grant delivery from or to the clearing house/clearing corporation:
    a. Regardless of the trade's value, accept the purchasing broker's partial delivery of shares resulting from the transaction.
    b. Accept shares resulting from a deal in at least two partial deliveries from the purchasing broker, with the first partial delivery being at least 50% of the

overall trade size. According to the rules of the stock exchange through which the deal was made, the delivery of the shares of the second partial delivery must be completed.

c. If any customer has reservations about accepting a partial settlement, bring such reservations to the SEBI's attention.
d. Pay for all shares supplied up to 5.30 p.m. on day 1 by 10 a.m. on day 3, allowing the broker to complete high value clearing on day 3.
e. Deliver stocks to brokers within 24 hours of the broker's availability of clear money or within 48 hours of the broker's receipt of payment through a high value check, pay order, or demand draft, whichever comes first.
f. When collateral is required for shares that are released to the broker to correct a faulty delivery, the collateral should be appropriate in relation to the percentage of the wrong delivery, and for cash-based collateral, interest would be provided to the broker by the custodian.

Indian Stock Holding Corporation Ltd.

SHCIL, or Stock Holding Corporation of India Ltd., was established in 1986 as a public limited company. Leading banks and financial institutions, including IFCI Ltd., IDBI Bank Ltd., SU-UTI, LIC, GIC, NIA, NIC, UIC, and TOICL, who are all market leaders in their respective industries, have jointly promoted and acquired ownership of it. SHCIL initially provided custodial and post trading services before gradually expanding its portfolio to include depository services and other services. SHCIL has made a name for itself in India as a supplier of comprehensive financial services solutions.

Institutions of finance

The financial sector is essential to a country's overall growth. The financial institutions are the sector's most significant component because they serve as a conduit for the flow of funds from net savers to net borrowers, or from individuals who spend less than their income to those who do the opposite. In the past, the financial sector has been the main provider of long-term financing for the economy. These organizations provide a range of financial services and products to meet the various demands of the business sector. Additionally, they support new businesses, small and medium-sized businesses, as well as the industries founded in underdeveloped regions.

Banking Institutions of finance

The term bank is derived from the Italian word banco, which means desk or bench. Florentine bankers used to conduct their business over a desk draped in a green fabric during the Renaissance. Nevertheless, evidence of financial activity dates back to ancient times. In truth, the word's roots may be found in the Ancient Roman Empire, when moneylenders would set up shop on a long bench called a "bancu" in the midst of walled courtyards called "macella," from which the terms "banco" and "bank" were formed. As a moneychanger, the businessman at the "bancu" essentially converted foreign cash into the Imperial Mint's coin, which was the sole form of legal tender in Rome.

Commercial Banking Means

Commercial banks have been noted to have two different meanings. The following are the two commonly used definitions of commercial banking:

1. To differentiate a regular bank from an investment bank (a kind of banking where the bank participates in the market investment process), the term "commercial bank" is employed.

What most people refer to as a "bank" is this. Some people use the phrase "commercial bank" to refer to banks that primarily serve businesses since the two types of banks are no longer required to be different corporations. The phrase "trading bank" was and is still used in several English-speaking nations outside of North America to refer to a commercial bank. The Glass-Steagall Act, which was passed by the U.S. Congress in 1933–1935 during the Great Depression and following the 1929 stock market crash, mandated that commercial banks only engage in banking activities (accepting deposits and making loans, as well as other fee-based services), whereas investment banks were restricted to capital markets activities. This division is no longer required. It generates money by obtaining deposits from customers and companies via time (or term) deposits, savings deposits, and checkable deposits. It provides loans to both households and companies. Government and business bonds are also purchased by it. Deposits make up its main liabilities, while loans and bonds make up its main assets.

2. A bank or branch of a bank that primarily deals with deposits and loans from companies or big enterprises as opposed to regular individual members of the public (retail banking) is referred to as commercial banking.

Commercial Banks Do

The following activities are carried out by commercial banks:

1. The act of processing payments using telegraphic transmission, EFTPOs, online banking, or other channels.
2. Issuing bank checks and drafts.
3. Taking deposits for term loans.
4. Making loans via overdrafts, installments, loans, or other loan types.
5. Offering guarantees, performance bonds, agreements to underwrite securities, documentary and standby letter of credit, and other "off balance sheet" liabilities.
6. Lockers or safe deposit boxes for the storage of papers and other goods.
7. The "financial supermarket" concept of selling, distributing, or brokering insurance, unit trusts, and other financial goods with or without advice.
8. In the past, major commercial banks also underwrote bonds and made markets in currency, interest rates, and securities connected to credit; however, in modern times, large commercial banks often have an investment bank arm that is engaged in the aforementioned operations.

Different Loans That Commercial Banks Issue

1**. Secured loan:**

A secured loan is one in which the borrower promises some asset as collateral (i.e., security) for the loan, such as a vehicle or piece of real estate.

2. **Mortgage loan:**

Used to buy real estate, a mortgage loan is a fairly popular sort of lending instrument. According to this agreement, the funds are utilized to buy the property. However, commercial banks are provided security a lien on the home's title until the mortgage is fully repaid. The bank would have the legal authority to seize the home and sell it in order to recoup any amounts owed to it in the event that the borrower defaulted on the loan. Commercial banks have historically had little interest in lending money for real estate and have invested only a tiny portion of their assets in mortgages. As their name would suggest, these financial

organizations derived the majority of their income from consumer and business loans and delegated the responsibility for house financing to other parties. Commercial banks are becoming more involved in mortgage lending, however, as a result of changes in banking rules and regulations. Commercial banks are now more free than ever to lend money for house mortgages because to changes in banking legislation. These banks engage in two major strategies when obtaining mortgages on real estate. First off, some banks have busy, structured divisions whose main responsibility is to aggressively compete for real estate loans. These banks serve as the primary provider of residential and agricultural mortgage loans in regions lacking specialist real estate banking institutions. Second, banks simply buy mortgages from mortgage bankers or dealers in order to obtain them. Dealer service firms, who were first employed by permanent lenders like commercial banks to get auto loans, also want to expand their operations outside their immediate region. However, in recent years, these businesses have focused primarily on amassing a large number of mobile home loans for both commercial banks and savings and loan organizations. These loans are often provided on a non-recourse basis by retail dealers to service providers. Almost all bank and service business contracts include a credit insurance clause that protects the lender in the event of a failure by the borrower.

Different Types of Banking are Common in India

1. Branch banking:

With this approach, a single bank does business via a network of branches spread throughout the nation. In India, the majority of scheduled commercial banks use a branch banking model to do business.

2. Unit banking:

With this system, banking is done via a single office that has been authorized to operate in a certain location.

3. Correspondent banking is a system in which banks agree to conduct banking transactions with other domestic or foreign banks.

Bank nationalization in India

The Indian banking sector had grown to be a crucial factor in the growth of the Indian economy by the 1960s. At the same time, it had grown to be a significant employer, and a discussion regarding the potential of nationalizing the banking sector had started. In a presentation titled "Stray Thoughts on Bank Nationalization," then-Indian Prime Minister Indira Gandhi stated the government's aim to the All-India Congress Meeting's annual convention. The publication was well-received and enthusiastically embraced. The GOI then adopted an order and nationalized the 14 major commercial banks with effect as of midnight on July 19, 1969, as a result of her quick and abrupt action. Indian nationalist Jayaprakash Narayan called the action a "masterstroke of political sagacity." The Banking Companies (Acquisition and Transfer of Undertaking) Bill was enacted by the Parliament two weeks after the ordinance was issued, and it was approved by the president on August 9 of the same year. In 1980, six further commercial banks were nationalized again. The government wanted greater control over how credit is distributed, which was the claimed justification for nationalization. Approximately 91% of India's banking industry was under the GOI's hands after the second phase of nationalization. Later, in 1993, the government combined Punjab National Bank and New Bank of India. The number of nationalized banks dropped from 20 to 19 as a consequence of the one and only merger between nationalized banks. The

nationalized banks expanded after this, up until the 1990s, at a rate of around 4%, which was closer to the average growth rate of the Indian economy.

CONCLUSION

In conclusion, in order to increase investor trust and maintain the integrity of India's financial markets, SEBI's auditing and supervision of custodians is essential. The financial system is made more resilient and stable overall because to SEBI's thorough custodial operations supervision.

For their part, custodians must place a high priority on regulatory compliance, risk management, and transparency in order to continue playing a vital role in enabling safe and effective investing operations.

SEBI is dedicated to fostering an environment that promotes investor protection, market integrity, and sustainable development in the Indian financial industry via constant vigilance and flexibility.

SEBI's dedication to custodian monitoring and auditing strengthens its position as a watchful regulatory body committed to defending investor interests and upholding market confidence. In order to address changing market dynamics, adopt best practices, and improve investor protection, cooperation between SEBI, custodians, and other stakeholders is essential.

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