INTRODUCTION OF INDIAN FINANCIAL SYSTEM

Meaning of Indian financial system

The financial system enables lenders and borrowers to exchange funds. India has a financial system that is controlled by independent regulators in the sectors of insurance, banking, capital markets and various services sectors.

Thus, a financial system can be said to play a significant role in the economic growth of a country by mobilizing the surplus funds and utilizing them effectively for productive purposes.

FEATURES OF INDIAN FINANCIAL SYSTEM:

- *It plays a vital role in economic development of a country.*
- *It encourages both savings and investment.*
- *It links savers and investors.*
- *It helps in capital formation.*
- *It helps in allocation of risk.*
- *It facilitates expansion of financial markets.*

COMPONENTS/ CONSTITUENTS OF INDIAN FINANCIAL SYSTEM

The following are the four major components that comprise the Indian Financial System:

1. *Financial Institutions*
2. *Financial Markets*
3. *Financial Instruments/ Assets/ Securities*

4. *Financial Services.*

COMPONENT IS DISCUSSED BELOW:

FINANCIAL INSTITUTIONS

Financial institutions are the intermediaries who facilitate smooth functioning of the financial system by making investors and borrowers meet. They mobilize savings of the surplus units and allocate them in productive activities promising a better rate of return. Financial institutions also provide services to entities (individual, business, government) seeking advice on various issue ranging from restructuring to diversification plans. They provide whole range of services to the entities who want to raise funds from the markets or elsewhere.

Financial institutions are also termed as financial intermediaries because they act as middle between savers by accumulating Funds them and borrowers by lending these fund.

It is also act as intermediaries because they accept deposits from a set of customers (savers lend these funds to another set of customers (borrowers). Like - wise investing institutions such ICCIC, mutual funds also accumulate savings and lend these to borrowers, thus perform the role of financial intermediaries.

TYPES OF FINANCIAL INSTITUTIONS

Financial institutions can be classified into two categories:

A. *Banking Institutions*

B. *Non - Banking Financial Institutions*

A. *BANKING INSTITUTIONS (Reserve Bank of India)*

Indian banking industry is subject to the control of the Central Bank. The RBI as the apex institution organises, runs, supervises, regulates and develops the monetary system and the financial system of the country. The main legislation governing commercial banks in India is the Banking Regulation Act, 1949.

The Indian banking institutions can be broadly classified into two categories:

1. *Organised Sector*
2. *Unorganised Sector.*

1. *Organised Sector*

The organised banking sector consists of commercial banks, cooperative banks and the regional rural banks.

***(a) Commercial Banks**: The commercial banks may be scheduled banks or non – scheduled banks. At present only one bank is a non - scheduled hank. All other banks are schedule banks. The commercial banks consist of 27 public sector banks, private sector banks and foreign banks. Prior to 1969, all major banks with the exception of State Bank of India in the private sector. An important step towards public sector banking was taken in July 1969, when 14 major private banks with a deposit base of 50 crores or more were nationalised. Later in 1980 another 6 were nationalised bringing up the total number banks nationalised to twenty.*

***(b) Co-operative banks:** An important segment of the organized sector of Indian banking is the co-operative banking. The segment is represented by a group of societies registered under the Acts of the states relating to co-operative societies. In fact, co-operative societies may be credit societies* *or non-credit societies.*

Different types of co-operative credit societies are operating in Indian economy. These institutions can be classified into two broad categories: (a) Rural credit societies which are primary agriculture, (b) Urban credit societies which are primarily non-agriculture.

For the purpose of agriculture credit there are different co-operative credit institutions to meet different kinds of needs.

(c) Regional Rural Banks (RRBs): *Regional Rural Banks were set by the state government and sponsoring commercial banks with the objective of developing the rural economy. Regional rural banks provide banking services and credit to small farmers, small entrepreneurs in the rural areas. The regional rural banks were set up with a view to provide credit facilities to weaker sections. They constitute an important part of the rural financial architecture in India. There were 196 RRBs at the end of June 2002, as compares to 107 in 1981 and 6 in 1975.*

(d) Foreign Banks: *Foreign banks have been in India from British days. Foreign banks as banks that have branches in the other countries and main Head Quarter in the Home Country. With the deregulation (Elimination of Government Authority) in 1993, a number of foreign banks are entering India. Foreign Banks are: Citi Bank. Bank of Ceylon.*

*2. **Unorganised Sector.***

In the unorganised banking sector are the Indigenous Bankers, Money Lenders.

*1. **Indigenous Bankers***

Indigenous Bankers are private firms or individual who operate as banks and as such both receive deposits and given loans. Like bankers, they also financial intermediaries. They should be distinguished professional money *lenders whose primary business is not banking and money lending. The indigenous banks are trading with the Hundies, Commercial Paper.*

1. ***Money Lenders:***

Money lenders depend entirely to on their one funds. Money Lenders may be rural or urban, professional or non-professional. They include large number of farmer, merchants, traders. Their operations are entirely unregulated. They charge very high rate of interst.

B. ***NON - BANKING INSTITUTIONS***

The non - banking institutions may be categorized broadly into two groups:

(a) Organised Non - Banking Financial Institutions.

(b) Unorganised Non - Banking Financial Institutions.

(a) Organised Non - Banking Financial Institutions

The organised non - banking financial institutions include:

1. ***Development Finance Institutions.***

These include: The institutions like IDBT, ICICI, IFCI, IIBI, IRDC at all India level. The State Finance Corporations (SFCs), State Industrial Development Corporations (SIDCs) at the state level.

Agriculture Development Finance Institutions as NABARD,LDBS etc.

Development banks provide medium and long term finance to the corporate and industrial sector and also take up promotional activities for economic development

2. ***Investment Institutions.***

These include those financial institutions which mobilise savings at the public at large through various schemes and invest these funds in corporate and government securities. These include LIC, GIC, LTT, and mutual funds.

The non - banking financial institutions in the organised sector) have been discussed at length in detail in separate chapters of this book.

(b) Unorganised Non - Banking Financial Institutions:
The unorganised non - banking financial institutions include number of non - banking financial companies (NBFCs) providing whole range of financial services. These include hire - purchase 300 consumer finance companies, leasing companies, housing finance companies, factoring companies, Credit rating agencies, merchant banking companies etc. NBFCs mobilise public funds and provide loanable funds.

FINANCIAL MARKET

It is through financial markets and institutions that the financial system of an economic works. Financial markets refer to the institutional arrangements for dealing in financial assets and credit instruments of different types such as currency, cheques, bank deposits, bills, bonds etc.

Functions of financial markets are:

(i) To facilitate creation and allocation of credit and liquidity

(ii) To serve as intermediaries for mobilisaton of savings.

(iii) To assist the process of balanced economic growth.

(iv) To provide financial convenience.

(v) To cater to the various credit needs of the business houses.

These organised markets can be further classified into two they are

(i) Capital Market

(ii) Money Market

CAPITAL MARKET

The capital market is a market for financial assets which have a long or indefinite maturity. Generally, it deals with long term securities which have *a maturity period of above one year. Capital market may be further divided into three namely:*

(I) Industrial securities market

(II) Government securities market and

(III) Long term loans market

*1. **INDUSTRIAL SECURITIES MARKET:***

As the very name implies, it is a market for industrial securities namely:
(i) Equity shares or ordinary shares,
(ii) Preference shares and
(iii) Debentures or bonds.

It is a market where industrial concerns raise their capital or debt by issuing appropriate instruments. It can be further subdivided into two. They are:
(i) Primary market or New issue market
(ii) Secondary market or Stock exchange

Primary Market

Primary market is a market for new issues or new financial claims. Hence, it is also called New Issue market. The primary market deals with those securities which are issued to the public for the first time.
In the primary market, borrowers exchange new financial securities for long term funds. Thus, primary market facilitates capital formation. There are three ways by which a company may raise capital in a primary market. They are:

(i) Public issue
(ii) Rights issue
(iii) Private placement

*The most common method of raising capital by new companies is through sale of securities to the public. It is called **public issue**. When an existing company wants to raise additional capital, securities are first offered to the existing shareholders on a pre-emptive basis. It is called **rights issue**. **Private placement** is a way of selling securities privately to a small group of investors.*

Secondary Market

Secondary market is a market for secondary sale of securities. In other words, securities which have already passed through the new issue market are traded in this market. Generally, such securities are quoted the Stock Exchange and it provides a continuous and regular market to buying and selling of securities. This market consists of all stock exchanges recognised by the Government of India. The stock exchanges in India are regulated under the Securities Contracts (Regulation) Act 1956. The Bombay Stock Exchange is the principal stock exchange in India which sets the tone of the other stock markets.

II. GOVERNMENT SECURITIES MARKET

It is otherwise called Gilt - Edged securities market. It is a market where Government securities are traded. In India there are many kinds of Government Securities - short term and long term. Long term securities are traded in this market while short term securities are traded in the money market. Securities issued by the Central Government, State Governments, Semi Government authorities like City Corporations, Port Trusts etc. Improvement Trusts, State Electricity Boards, All India and State level financial institutions and public sector enterprises are dealt in this market.

III. LONG TERM LOANS MARKET

Development banks and commercial banks play a significant role in this *market by supplying long term loans to corporate customers.*

Long term loans market may further be classified into:

(1) Term loans market

(ii) Mortgages market

(iii) Financial Guarantees market.

Term Loans Market

In India, many industrial financing institutions have been created by the Government both at the national and regional levels to supply long term and medium term loans to corporate customers directly as well as indirectly. These development banks dominate the industrial finance in India. Institutions like IDBI, IFCI, ICICI, and other financial corporations come under this category.

Mortgages Market

A mortgage loan is a loan against the security of immovable property like real estate. The transfer of interest in a specific immovable property to secure a loan is called mortgage. This mortgage may be equitable mortgage or legal one.

MONEY MARKET

Money market is a market for dealing with financial assets and securities which have a maturity period of upto one year. In other words, it is a market for purely short term funds. The money market may be subdivided into four. They are:

(i) Call money market

(ii) Commercial bills market

(iii) Treasury bilis market

(iv) Short term loan market.

Call Money Market

The call money market is a market for extremely short period loans say one day to fourteen days. So, it is highly liquid. The loans are repayable on demand at the option of either the lender or the borrower. In India, call money markets are associated with the presence of stock exchanges and hence, they are located in major industrial towns like Bombay, Calcutta, Madras, Delhi, Ahmedabad etc. The special feature of this market is that the interest rate varies from day to day and even from hour to hour and centre to centre. It is very sensitive to changes in demand and supply of call loans.

Commercial Bills Market

It is a market for Bills of Exchange arising out of genuine trade transactions. In the case of credit sale, the seller may draw a bill of exchange on the buyer. The buyer accepts such a bill promising to pay at a later date specified in the bill. The seller need not wait until the due date of the bill. Instead, he can get immediate payment by discounting the bill.

Treasury Bills Market

It is a market for treasury bills which have ' short - term ' maturity. A treasury bill is a promissory note or a finance bill issued by the Government.

It is highly liquid because its repayment is guaranteed by the Government. It is an important instrument for short term borrowing of the Government There are two types of treasury bills namely (i) ordinary or regular and (ii) ad hoc treasury bills popularly known as ' ad hocs'. ***Ordinary treasury bills*** *are issued to the public, banks and other financial institutions with a view to raising resources for the Central Government to meet its short term financial needs. Ad hoc treasury bills are issued in favour of the RBI only.*

They are not sold through tender or auction. They can be purchased by the RBI only. ***Ad hocs*** *are not marketable in India but holders of these bills can sell them back to RBI.*

Short - Term Loan Market

It is a market where short - term loans are given to corporate customers for meeting their working capital requirements. Commercial banks play a significant role in this market. Commercial banks provide short term loans in the form of cash credit and overdraft Over draft facility is mainly given to business people whereas cash credit is given to industrialists. Overdraft is purely a temporary accommodation and it is given in the current account itself. But cash credit is for a period of one year and it is sanctioned in a separate account.

FINANCIAL INSREUMENTS

Financial instruments refer to those documents which represents financial claims on assets. As discussed earlier, financial asset refers to a claim to a claim to the repayment of a certain sum of money at the end of a specified period together with interest or dividend. Examples: Bill of exchange, Promissory Note, Treasury Bill.

Financial securities can be classified into:

(i) Primary or direct securities.

(ii) Secondary or indirect securities.

Primary Securities

These are securities directly issued by the ultimate investors to the ultimate savers. Eg. shares and debentures issued directly to the public.

Secondary Securities

These are securities issued by some intermediaries called financial intermediaries to the ultimate savers. Eg. Unit Trust of India and mutual funds issue securities in the form of units to the public and the money pooled is invested in companies.

Again these securities may be classified on the basis of duration as follows:

(i) Short - term securities

(ii) Medium term securities

(iii) Long - term securities.

***Short - term securities** are those which mature within a period of one year. Eg, Bill of Exchange, Treasury bill, etc. **Medium term securities** are those which have a maturity period ranging between one and five years. Eg. Debentures maturing within a period of 5 years, **Long - term securities** are those which have a maturity period of more than five years. Eg, Government Bonds maturing after 10 years.*

FINANCIAL SERVICES

Efficiency of emerging financial system largely depends upon the quality and variety of financial services provided by financial intermediaries. The term financial services can be defined as "activities, benefits, and satisfactions, connected with the sale of money, that offer to users and customers, financial related value. within the financial services industry the main sectors are banks, financial institutions, and non-banking financial companies.

KINDS OF FINANCIAL SERVICES

Financial services provided by various financial institutions, commercial banks and merchant bankers can be broadly classified into two categories.

1. *Asset based/fund based services.*
2. *Fee based/advisory services.*

Asset based/fund based services

The asset/ fund based services provided by banking and non - banking financial institutions as discussed below briefly.

1. ***Equipment Leasing/ Lease Financing***

Leasing is a arrangement that provides a firm with the use and control over assets without buying and owning the same. It is a form of renting assets. However, in making an investment, the firm need not own the asset. It is basically interested in acquiring the use of the asset. Thus, the firm may consider leasing of the asset rather than buying it.

In comparing leasing with buying, the cost of leasing the asset should be compared with the cost of financing the asset through normal sources of financing, i. e. debt and equity. Since payment of lease rentals is similar to payment of interest on borrowings and lease financing is equivalent to debt.

2. ***Hire Purchase and Consumer Credit***

Hire purchase means a transaction where goods are purchased and sold on the terms that (i) payment will be made it installments, (ii) the possession of the goods is given to the buyer immediately, (iii) the property ownership) in the goods remains with the vendor till the last installment is paid,(iv) the seller can repossess the goods in case of default in payment of any instalment, and (v) each instalment is treated as hire charges till the *last instalment is paid.*

***Consumer credit** includes all asset based financing plans offered to individuals to help them acquire durable consumer goods. In a consumer credit transaction the individual/ consumer/ buyer pays a part of the cash purchase price at the time of the delivery of the asset and pays the balance with interest over a specified period of time.*

3. *VENTURE CAPITAL*

*In the real sense, venture capital financing is one of the most recent entrants in the Indian capital market. There is a significant scope for venture capital companies in our country because of increasing emergence of technocrat entrepreneurs who lack capital to be risked. These **venture capital** companies provide the necessary risk capital to the entrepreneurs so as to meet the promoters contribution as required by the financial institutions. In addition to providing capital, these VCFS (venture capital firms) take an active interest in guiding the assisted firms.*

4. *Insurance Services*

Insurance is a contract where by the insurer e. insurance company agrees/ undertakes, in consideration of a sum of money (premium) to make good the loss suffered by the insured (policy holder) against a specified risk such as fire or compensate the beneficiaries (insured) on the happening of a specified event such as accident or death. The document containing the terms of contract, in black and white, between the insurer and the insured is called policy. The property which is insured is the subject matter of insurance. The interest which the insured has in the subject matter of insurance is known as insurable interest. Depending upon the subject matter, insurance services are divided into (i) life (ii) general.

5. *Factoring*

Factoring, as a fund based financial service provides resources to finance *receivables as well as it facilitates the collection of receivables. It is another method of raising short - term finance through account receivable credit offered by commercial banks and factors.*

A commercial bank may provide finance by discounting the bills or invoices of its customers. Thus, a firm gets immediate payment for sales made on credit. A factor is a financial institution which offers services relating to management and financing of debts arising out of credit sales.

B. FEE BASED ADVISORY SERVICES

(i) ***Merchant Banking***

Fee based advisory services includes all these financial services rendered by Merchant Bankers. Merchant bankers play an important role in the financial services Sector. The Industrial Credit and Investment Corporation of India (ICICI) was the first development finance institution to initiate such service in 1974. After mid - seventies, tremendous growth in the number of merchant banking organisations les taken place. These include banks financial institutions, ***non - banking financial companies (****NBFCS), brokers and so on. financial Services provided by these organisations include loan syndication portfolio management, corporate counselling project counselling debenture trusteeship, mergers acquisitions.*

(ii) ***Credit Rating***

Credit rating is the opinion of the rating agency on the relative ability and willingness of the issuer of debt instrument to meet the debt service obligations as and when they arise. As a fee based financial advisory *service, credit rating useful to investors, corporates (borrowers), banks and financial institutions. For the investors, it is an indicator expressing the underlying credit quality of a (debt) issue programme. The investor is fully formed about the company as any effect of changes in business/ economic conditions on the agency company is evaluated and published regularly by the rating agency.*

(iii) ***Stock - Broking***

Prior to the setting up of SEBI, stock exchanges were being supervised by the Ministry of Finance under the Securities Contracts Regulation Act (SCRA) and were operating more or less self-regulatory organisations.

The need to reform stock exchanges was felt, when malpractices crept into Trading and in order to protect investor's interests, SEBI was set up to ensure that stock exchange perform their self - regulatory role properly. Since then, stock broking has emerged as a professional advisory service Stockbroker is a member of a recognised stock exchange who buys, sells or deals in shares/ securities. It is mandatory for each stockbroker to get him/ herself registered with SEBI order to act as a broker. SEBI is empowered to impose conditions while granting the certificate of registration.

FINANCIAL MARKET

It is through financial markets and institutions that the financial system of an economic works. Financial markets refer to the institutional arrangements for dealing in financial assets and credit instruments of different types such as currency, cheques, bank deposits, bills, bonds etc. Financial market classified into two they are:

(i) Money Market

(ii)Capital Market

(I) MONEY MARKET

Money market is a market for dealing with financial assets and securities which have a maturity period of upto one year. In other words, it is a market for purely short term funds.

The importance/functions of the money market is highlighted as under:

*1. **Economic development**: The money market provides short term funds to both public and private institutions. These institutions need money to finance their capital needs.*

In other words, the money market assures supply of funds; the financing is done through discounting of the trade bills, commercial banks, acceptance houses, discount houses and brokers. In this way, the money market helps in the economic development by providing financial help to trade, commerce and industry. The businessmen take advantage by investing their cash in highly liquid assets to earn income and also to enjoy liquidity because these assets can be converted into cash without much difficulty.

*2. **Profitable investment**: The commercial banks deal with the deposits of their customers. The banks are required to put their assets into cash form to meet the directions of the central bank on the one hand, while on the other, they have to put their excess reserves into productive channels to earn income on them. The aim of the commercial banks is to maximize profits. The excess reserves of the banks are invested in near money assets.*

*3. **Borrowings by the government**:*

The money market helps the government in borrowing short term funds at very low interest rates. The borrowing is done on the basis of treasury bills. But in case the government resorts to deficit financing or to print more currency or to short term funds at the money supply over and above the borrow from the central bank, it will merely raise Thus it is clear that the needs of the economy and hence the price level will boost up. Money *market is very useful for the government since it meets its financial needs.*

*4. **Importance for central bank:***

If the money market is well - developed, the central bank implements the monetary policy successfully. It is only through the money market that the central bank can control the banking system and thus contribute to the development of trade and commerce. The money market is very sensitive a change in one sub – market affects the other sub - markets immediately. It means the central bank can affect the whole money market by changing just one sub - market.

*5. **Mobilisation of funds:***

The money market helps in transferring funds from one sector to another. The development of any economy depends on availability of finance. No country can develop its trade, commerce and industry until and unless the financial resources are mobilized.

*6. **Savings and investment***

The money market is that it helps in promoting liquidity and safety of financial assets. By doing so it can help in encouraging savings and investment. The saving and investment equilibrium of demand and supply of loanable funds helps the allocation of resources.

CAPITAL MARKET

The capital market is a market for financial assets which have a long or indefinite maturity. Generally, it deals with long term securities which have a maturity period of above one year.

FUNCTIONS OF CAPITAL MARKET

' The major functions performed by a capital/ security market are:

1. ***Helps in capital formation.***

The capital market plays an important role in mobilisation of savings and channel them into productive investments for the development of commerce and industry. As such, the capital market helps in capital formation and economic growth of the country.

2. ***Act as link between savers and investors.***

The capital market acts as an important link between savers and investors. The savers are lenders of funds while investors are borrowers of funds. The savers who do not spend all their income are called "Surplus units" and the borrowers are known as " deficit units. The capital market is the transmission mechanism between surplus units and deficit units. It is a conduit through which surplus unity lend their surplus funds to deficit units.

3. ***Helps in increasing national income.***

Funds come into the capital market from individuals and financial intermediaries and are used by commerce, industry and government. It thus facilitates the transfer of funds to be used more productively and profitability to increases the national income.

4. ***Facilitates buying and selling.***

Surplus units buy securities with their surplus funds and deficit wits ells securities to raise the funds they need. Funds flow from lenders to borrowers either directly or indirectly through financial institutions such as banks, unit trusts, mutual funds, etc. The borrowers issue primary securities which are purchased by lenders either directly or indirectly through financial institutions.

5. ***Channelizes funds from unproductive to productive resources.***

The capital market provides a market mechanism for those who have savings and to those who need funds for productive investments. It divers *resources from wasteful and unproductive channels such as gold, jewellery, real estate, conspicuous consumption, etc, to productive investments*

*6. **Minimises speculative activities**.*

It does so by providing capital to the needy al reasonable interest rates and helps in minimising speculative activities.

*7. **Brings stability in value of stocks**.*

A well - developed capital market comprising expert banking and non - banking intermediaries brings stability in the value of stocks and securities..

*8. **Promotes economic growth.** The capital market encourages economic growth. The various institutions which operate in the capital market give quantities and qualitative direction to the flow of funds and bring rational allocation of resources. They do so by converting financial assets into productive physical assets. This leads to the development of commerce and industry through the private and public sector, thereby inducing economic growth.*

Primary Market / New Issue Market

Primary market is a market for new issues or new financial claims. Hence, it is also called New Issue market. The primary market deals with those securities which are issued to the public for the first time.

In the primary market, borrowers exchange new financial securities for long term funds. Thus, primary market facilitates capital formation. There are three ways by which a company may raise capital in a primary market.

FEATURES OF PRIMARY MARKETS

(i) This is the market for new long term equity capital. The primary market is the market where the securities are sold for the first time. Therefore it is also called the new issue market (NIM).

(ii) in a primary issue, the securities are issued by the company directly to investors.

(iii) The company receives the money and issues new security certificates to the investors

(iv) Primary issues are used by companies for the purpose of setting up new business or for expanding or modernizing the existing business.

(v) The primary market performs the crucial function of facilitating capital formation in the economy.

(vi) The new issue market does not include certain other sources of new long term external

finance, such as loans from financial institutions. Borrowers in the new issue market may be raising capital for converting private capital into public capital, this is known as " going public. "

FUNCTIONS OF NEW ISSUE MARKET

A three service functions:

The main functions of a new issue sue market can divided into new project.

1. ***Origination.***

It refers to the work of investigation analysis and processing of new project proposals.. It starts before an issue is actually floated in the market. This function is done by merchant bankers who may be commercial banks, all India financial institutions or private firms. At present, financial institutions and private firms also perform this service is highly important the success of the issue depends, to a large extent on the efficiency of the market.

2. ***Underwriting.***

It is an agreement whereby the underwriter promises to subscribe to specified number of shares or debentures or a specified amount of stock in the event of public not subscribing to the issue. If the issue is fully subscribed, then there is no liability for the underwriter. If a part of share issues remains unsold, the underwriter will buy the shares. Thus, underwriting is a guarantee for marketability of shares. There are two types of underwriters in India - Institutional (LIC, UTI, IDBI, ICICI) and Non - institutional are brokers.

3. ***Distribution.***

It is the function of sale of securities to ultimate investors. This service is performed by specialized agencies like brokers and agents who maintain a regular direct contact with the ultimate investors.

Secondary Market/Stock Exchange Market

Secondary market is a market for secondary sale of securities. In other words, securities which have already passed through the new issue market are traded in this market. Generally, such securities are quoted the Stock Exchange and it provides a continuous and regular market to buying and selling of securities. This market consists of all stock exchanges recognised by the Government of India. The stock exchanges in India are regulated under the Securities Contracts (Regulation) Act 1956. The Bombay Stock Exchange is the principal stock exchange in India which sets the tone of the other stock markets.

FUNCTIONS OF STOCK EXCHANGE

The stock exchanges play an important role in the economic development of a country.

***The importance of stock exchange will be clear from the functions they perform and discussed**:*

as follows: provide a place where shares and stock

*1. **Ensure Liquidity of Capital**.*

The stock exchanges where buyers and sellers are converted into cash. The exchanges provide a ready market. Had are always available and those who are in need of hard cash can sell their holdings this not been possible then many persons would have feared for blocking their savings in Securities as they can not again convert them into cash.

*2. **Continuous Market for Securities.***
The stock exchanges provide a ready market in securities. The securities once listed continue to be traded at the exchanges irrespective the fact that owners go on changing. The exchanges provide a regular market for trading in securities.

*3. **Mobilising Surplus Savings**.*

The stock exchanges provide a ready market for various securities. The investors do not have any difficulty in investing their savings by purchasing shares, bonds etc, from the exchanges. If this facility is not there then many persons who want to invest their savings will not find avenues to do so. In this way stock exchanges play an important role in mopping up surplus funds of investors.

*4. **Helpful in Raising New Capital**.*

The new and existing concerns need capital for their activities. The new concerns raise capital for the first time and existing units increase their capital for expansion and diversification purposes. The shares of new concerns are registered at stock exchanges and existing companies also sell their shares through brokers etc, at exchanges. The exchanges are helpful in raising capital both by nets old concerns.

*5. **Safety in Dealings**.*

The dealings at stock exchanges are governed by well - defined rules and regulations of Securities Contract (Regulation) Act, 1956. There is no scope manipulating transactions. Every contact is done according to the procedure laid down and there is no fear in the minds of contracting parties. The safety in dealings brings confidence in the minds of all concerned parties and helps in increasing various dealings.

*6. **Listing of Securities**.*

Only listed securities can be purchased at stock exchanges. Every company desirous of listing its securities will apply to the exchange authorities. The listing is allowed only after a critical examination of capital structure, management and prospects of the company. The listing of securities gives privilege to the company. The investors can form their own views about the *securities because listing a security does not guarantee the financial stability of the company.*

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7. ***Smoothens the Price Movements.***

A stock exchange smoothens the price movements of stocks in the market by ensuring a continuous flow of securities,

8. ***Investor Protection.***

The stock exchange renders safeguarding activities for investors in securities. It provides a grievance redressal mechanism for investors. Stock exchanges also operate a compensation fund for the protection of investors.

MONEY MARKET

Money market is a market for dealing with financial assets and securities which have a maturity period of up to one year. In other words, it is a market for purely short term funds. The money market may be subdivided into four. They are:

Objectives of Money Market

The following are the important objectives of a money market:

(i) To provide a parking place to employ short-term surplus funds.

(ii) To provide room for overcoming short-term deficits.

(iii) To enable the Central Bank to influence and regulate liquidity in the economy through its intervention in this market.

(iv) To provide a reasonable access to users of Short-term funds to meet their requirements quickly, adequately and at reasonable costs.

(v) To give a sensible access to clients of here and now assets to meet their prerequisite rapidly, sufficiently at sensible cost.

(vi) To give a stopping spot to utilize here and now surplus assets.

COMPOSITION/COMPONENTS OF MONEY MARKET

(i) Call money market

(ii) Commercial bills market

(iii) Treasury bills market

(iv) Short term loan market.

(v) Bill Discount Market

Call Money Market

The call money market is a market for extremely short period loans say one day to fourteen days. So, it is highly liquid. The loans are repayable on demand at the option of either the lender or the borrower. In India, call money markets are associated with the presence of stock exchanges and hence, they are located in major industrial towns like Bombay, Calcutta, Madras, Delhi, Ahmedabad etc. The special feature of this market is that the interest rate varies from day to day and even from hour to hour and centre to centre. It is very sensitive to changes in demand and supply of call loans.

Commercial Bills Market

It is a market for Bills of Exchange arising out of genuine trade transactions. In the case of credit sale, the seller may draw a bill of exchange on the buyer. The buyer accepts such a bill promising to pay at a later date specified in the bill. The seller need not wait until the due date of the bill. Instead, he can get immediate payment by discounting the bill.

Treasury Bills Market

It is a market for treasury bills which have ' short - term ' maturity. A treasury bill is a promissory note or a finance bill issued by the Government.

It is highly liquid because its repayment is guaranteed by the Government. It is an important instrument for short term borrowing of the Government There are two types of treasury bills namely (i) ordinary or regular and (ii) ad hoc treasury bills popularly known as ' ad hocs'. ***Ordinary treasury bills*** *are issued to the public, banks and other financial institutions with a view to raising resources for the Central Government to meet its short term financial needs. Ad hoc treasury bills are issued in favour of the RBI only. They are not sold through tender or auction. They can be purchased by the*

RBI only. ***Ad hocs*** *are not marketable in India but holders of these bills can sell them back to RBI.*

Short - Term Loan Market

It is a market where short - term loans are given to corporate customers for meeting their working capital requirements. Commercial banks play a significant role in this market. Commercial banks provide short term loans in the form of cash credit and overdraft Over draft facility is mainly given to business people whereas cash credit is given to industrialists. Overdraft is purely a temporary accommodation and it is given in the current account itself. But cash credit is for a period of one year and it is sanctioned in a separate account.

BILL OF EXCHANGE

A written, unconditional order by one party (the drawer) to another (the drawee) to pay a certain sum, either immediately (a sight bill) or on a fixed date (a term bill), for payment of goods and/or services received. The drawee accepts the bill by signing it, thus converting it into a post-dated check and a bindingcontract.
a bill of exchange contains: (1) The term bill of exchange inserted in the body of the instrument and expressed in the language employed in drawing up the instrument.(2) An unconditional order to pay a determinate sum of money. (3) The name of the person who is to pay (drawee). (4) A statement of the time of payment. (5) A statement of the place where payment is to be made. (6) The name of the person to whom or to whose order payment is to be made. (7) A statement of the date and of the place where the bill is issued. (8) The signature of the person who issues the bill (drawer). A bill of exchange is the most often used form of payment in local and international trade, and has a long history- as long as that of writing

Types Of Money Market Instruments

Treasury Bills (T-Bills)

Issued by the Central Government, Treasury Bills are known to be one of the safest money market instruments available. However, treasury bills carry zero risk. I.e. are zero risk instruments. Therefore, the returns one gets on them are not attractive. Treasury bills come with different maturity periods like 3-month, 6-month and 1 year and are circulated by primary and secondary markets. Treasury bills are issued by the Central government at a lesser price than their face value.

The interest earned by the buyer will be the difference of the maturity value of the instrument and the buying price of the bill, which is decided with the help of bidding done via auctions. Currently, there are 3 types of treasury bills issued by the Government of India via auctions, which are 91-day, 182-day and 364-day treasury bills.

Certificate of Deposits (CDs)

A Certificate of Deposit (CD) is a time deposit with bank. CDs are generally issued by commercial banks but the can be bought through brokerages. • They bear a specific maturity date (from three months to five years, a specified interest rate and can be issued in any denomination. • CDs offer a slightly higher yield than T-Bills because of the slightly higher default risk for bank.

Commercial Papers (CPs)

Commercial Papers are can be compared to an unsecured short-term promissory note which is issued by highly rated companies with the *purpose of raising capital to meet requirements directly from the market. CPs usually feature a fixed maturity period which can range anywhere from 1 day up to 270 days. Highly popular in countries like Japan, UK, USA, Australia and many others, Commercial Papers promise higher returns as compared to treasury bills and are automatically not as secure in comparison. Commercial papers are actively traded in secondary market.*

Repurchase Agreements (Repo)

Repurchase Agreements, also known as Reverse Repo or simply as Repo, loans of a short duration which are agreed upon by buyers and sellers for the purpose of selling and repurchasing. These transactions can only be carried out between RBI approved parties Repo / Reverse Repo transactions can be done only between the parties approved by RBI. Transactions are only permitted between securities approved by the RBI like treasury bills, central or state government securities, corporate bonds and PSU bonds.

Banker's Acceptance (BA)

Banker's Acceptance or BA is basically a document promising future payment which is guaranteed by a commercial bank. Similar to a treasury bill, Banker's Acceptance is often used in money market funds and specifies the details of the repayment like the amount to be repaid, date of repayment and the details of the individual to which the repayment is due. Banker's Acceptance features maturity periods ranging between 30 days up to 180 days.

BILL OF EXCHANGE

BILLS OF EXCHANGE Bills of exchange are similar to checks and promissory notes. They can be drawn by individuals or banks and are generally transferable by endorsements. The difference between a promissory note and a bill of exchange is that this product is transferable and can bind one party to pay a third party that was not involved in its *creation. If these bills are issued by a bank, they can be referred to as bank drafts. If they are issued by individuals, they can be referred to as trade drafts.*

STOCK MARKETS

Primary Market / New Issue Market

Primary market is a market for new issues or new financial claims. Hence, it is also called New Issue market. The primary market deals with those securities which are issued to the public for the first time.

In the primary market, borrowers exchange new financial securities for long term funds. Thus, primary market facilitates capital formation. There are three ways by which a company may raise capital in a primary market.

FEATURES OF PRIMARY MARKETS

(i) This is the market for new long term equity capital. The primary market is the market where the securities are sold for the first time. Therefore it is also called the new issue market (NIM).

(ii) in a primary issue, the securities are issued by the company directly to investors.

(iii) The company receives the money and issues new security certificates to the investors

(iv) Primary issues are used by companies for the purpose of setting up new business or for expanding or modernizing the existing business.

(v) The primary market performs the crucial function of facilitating capital formation in the economy.

(vi) The new issue market does not include certain other sources of new long term external

finance, such as loans from financial institutions. Borrowers in the new issue market may be raising capital for converting private capital into public capital, this is known as " going public. "

FUNCTIONS OF NEW ISSUE MARKET

A three service functions:

The main functions of a new issue sue market can divided into new project.

1. ***Origination.***

It refers to the work of investigation analysis and processing of new project proposals.. It starts before an issue is actually floated in the market. This function is done by merchant bankers who may be commercial banks, all India financial institutions or private firms. At present, financial institutions and private firms also perform this service is highly important the success of the issue depends, to a large extent on the efficiency of the market.

2. ***Underwriting.***

It is an agreement whereby the underwriter promises to subscribe to specified number of shares or debentures or a specified amount of stock in the event of public not subscribing to the issue. If the issue is fully subscribed, then there is no liability for the underwriter. If a part of share issues remains unsold, the underwriter will buy the shares. Thus, underwriting is a guarantee for marketability of shares. There are two types of underwriters in India - Institutional (LIC, UTI, IDBI, ICICI) and Non - institutional are brokers.

3. ***Distribution.***

It is the function of sale of securities to ultimate investors. This service is performed by specialized agencies like brokers and agents who maintain a regular direct contact with the ultimate investors.

PLAYERS IN THE NEW ISSUE MARKET

There are many players in the new issue market. The important them are the following:

1. *Merchant Bankers*
2. *Registrars*
3. *Collecting and co - ordinating bankers*
4. *Underwriters and brokers*
5. *Printers, advertising agencies and mailing agencies.*

*1. **Merchant Bankers***

They are the issue managers, lead managers, co - managers and are responsible to the company and SEBI. Their functions and working are described in a separate chapter.

*2. **Registrars to the Issue***

Registrars are an important category of intermediaries who undertake all activities connected with new issue management. They are appointed by the company in consultation with the merchant bankers to the issue. Registrars have a major role, next to merchant bankers, in respect of servicing of investors. The role of Registrar in the pre - issue, during the currency of issue, pre allotment, allotment and post allotment are described below:

Role of Registrar in Pre - issue

1. *Suggest draft application form to the merchant bankers.*
2. *Help identifying the collection centres. The choice of collection centre and of collecting banker is critical to the success of the issue.*
3. *Assist in opening collection accounts with banks and lay down*

procedure for operation of these accounts. Send instructions to collecting branches, for collection of application along with cheques, drafts, stock invest separately and remittance of funds.

4. *Workout modalities to receive the collection figures on a regular basis until the subscription list is closed. and expertise, quality of manpower, their track record, adequacy of infrastructure such as computers, storage space etc. and capital adequacy.*

3. ***Collecting and Co - ordinating Bankers***

Collecting bankers collect the subscriptions in cash, cheques, stock invest etc. Co - ordinating bankers collect information on subscriptions and co-ordinate the collection work. They monitor the work and keep inform them to the registrars and merchant bankers. Collecting banker and coordinating banker may be the same bank or different banks.

4. ***Underwriters and Brokers***

The functions and role of underwriters are explained separately. Brokers along with the network of sub - brokers market the new issues. They send their own circulars and applications to the clients and do follow up work to market the securities.

5. ***Printers, advertising agencies and mailing agencies** are other Organisations involved in the new issue market operations.*

SECONDARY/STOCK MARKET

SECONDARY MARKET

Secondary market is a market for secondary sale of securities. In other words, securities which have already passed through the new issue market are traded in this market. Generally, such securities are quoted the Stock Exchange and it provides a continuous and regular market to buying and selling of securities. This market consists of all stock exchanges recognised by the Government of India. The stock exchanges in India are regulated under the Securities Contracts (Regulation) Act 1956. The Bombay Stock Exchange is the principal stock exchange in India which sets the tone of the other stock markets.

FUNCTIONS OF STOCK EXCHANGE

The stock exchanges play an important role in the economic development of a country.

***The importance of stock exchange will be clear from the functions they perform and discussed**:*

as follows: provide a place where shares and stock

*1. **Ensure Liquidity of Capital**.*

The stock exchanges where buyers and sellers are converted into cash. The exchanges provide a ready market. Had are always available and those who are in need of hard cash can sell their holdings this not been possible then many persons would have feared for blocking their savings in Securities as they can not again convert them into cash.

*2. **Continuous Market for Securities.***
The stock exchanges provide a ready market in securities. The securities once listed continue to be traded at the exchanges irrespective the fact that owners go on changing. The exchanges provide a regular market for

trading in securities.

3. ***Mobilising Surplus Savings.***

The stock exchanges provide a ready market for various securities. The investors do not have any difficulty in investing their savings by purchasing shares, bonds etc, from the exchanges. If this facility is not there then many persons who want to invest their savings will not find avenues to do so. In this way stock exchanges play an important role in mopping up surplus funds of investors.

4. ***Helpful in Raising New Capital.***

The new and existing concerns need capital for their activities. The new concerns raise capital for the first time and existing units increase their capital for expansion and diversification purposes. The shares of new concerns are registered at stock exchanges and existing companies also sell their shares through brokers etc, at exchanges. The exchanges are helpful in raising capital both by nets old concerns.

5. ***Safety in Dealings.***

The dealings at stock exchanges are governed by well - defined rules and regulations of Securities Contract (Regulation) Act, 1956. There is no scope manipulating transactions. Every contact is done according to the procedure laid down and there is no fear in the minds of contracting parties. The safety in dealings brings confidence in the minds of all concerned parties and helps in increasing various dealings.

6. ***Listing of Securities.***

Only listed securities can be purchased at stock exchanges. Every company desirous of listing its securities will apply to the exchange authorities. The listing is allowed only after a critical examination of capital structure, *management and prospects of the company. The listing of securities gives privilege to the company. The investors can form their own views about the securities because listing a security does not guarantee the financial stability of the company.*

.7. Smoothens the Price Movements.

A stock exchange smoothens the price movements of stocks in the market by ensuring a continuous flow of securities,

8. Investor Protection.

The stock exchange renders safeguarding activities for investors in securities. It provides a grievance redressal mechanism for investors. Stock exchanges also operate a compensation fund for the protection of investors.

Listing of Securities

Objectives | Requirements | Procedure

Listing of Securities

Listing means the admission of securities of a company to trading on a stock exchange. Listing is not compulsory under the Companies Act. It becomes necessary when a public limited company desires to issue shares or debentures to the public. When securities are listed in a stock exchange, the company has to comply with the requirements of the exchange.

Objectives of Listing

The major objectives of listing are

1. *To provide ready marketability and liquidity of a company's securities.*
2. *To provide free negotiability to stocks.*
3. *To protect shareholders and investors interests.*

4. To provide a mechanism for effective control and supervision of trading.

Listing requirements

A company which desires to list its shares in a stock exchange has to comply with the following requirements:

1. Permission for listing should have been provided for in the Memorandum of Association and Articles of Association.

2. The company should have issued for public subscription at least the minimum prescribed percentage of its share capital (49 percent).

3. The prospectus should contain necessary information with regard to the opening of subscription list, receipt of share application etc.

4. Allotment of shares should be done in a fair and reasonable manner. In case of over subscription, the basis of allotment should be decided by the company in consultation with the recognized stock exchange where the shares are proposed to be listed.

5. The company must enter into a listing agreement with the stock exchange. The listing agreement contains the terms and conditions of listing. It also contains the disclosures that have to be made by the company on a continuous basis.

Minimum Public Offer

A company which desires to list its securities in a stock exchange, should offer at least sixty percent of its issued capital for public subscription. Out of this sixty percent, a maximum of eleven percent in the aggregate may be reserved for the Central government, State government, their investment agencies and public financial institutions.

The public offer should be made through a prospectus and through *newspaper advertisements. The promoters might choose to take up the remaining forty percent for themselves, or allot a part of it to their associates.*

Fair allotment

Allotment of shares should be made in a fair and transparent manner. In case of over subscription, allotment should be made in an equitable manner in consultation with the stock exchange where the shares are proposed to be listed.

In case, the company proposes to list its shares in more than one exchange, the basis of allotment should be decided in consultation with the stock exchange which is located in the place in which the company's registered office is located.

Listing Procedure

The following are the steps to be followed in listing of a company's securities in a stock exchange:

1. *The promoters should first decide on the stock exchange or exchanges where they want the shares to be listed.*

2. *They should contact the authorities to the respective stock exchange/ exchanges where they propose to list.*

3. *They should discuss with the stock exchange authorities the requirements and eligibility for listing.*

4. *The proposed Memorandum of Association, Articles of Association and Prospectus should be submitted for necessary examination to the stock exchange authorities*

5. *The company then finalizes the Memorandum, Articles and Prospectus*

6. *Securities are issued and allotted.*

7. *The company enters into a listing agreement by paying the prescribed fees and submitting the necessary documents and particulars.*

8. *Shares are then and are available for trading.*

Bombay Stock Exchange

The Bombay Stock Exchange or BSE is an Indian stock exchange which is located at Dalal Street, Mumbai. It was established in the year 1875 and founded by Premchand Roychand, one of the influential businessmen in the 19th century. He was famously known as the Big Bull, the Bullion King or the Cotton King. He was also the founder of Stock Brokers Association, known as BSE and the Native Share.

Whilst Bombay Stock Exchange Ltd is now synonymous with Dalal Street, however, it was not always so. The very first venue of the earliest stock broker meetings was held in the 1850s under banyan trees, in-front of the Town Hall, where Horniman Circle is presently situated. A year later, the brokers moved to another venue, at the junction of Meadows Street which is now called Mahatma Gandhi Road. With an increase in the number of brokers, they had to shift from one place to another, this would end to overflowing the streets. Last, in the year 1874, the brokers found a permanent place which they can call their own. It was known as Dalal Street or Broker's Street.

The Bombay Stock Exchange or BSE is the oldest stock exchange in Asia. On 31st August 1957, The Bombay Stock Exchange became the first stock exchange that was recognized by the Government of India under the Securities Contracts Regulation Act.

Capital Market of India

Presently, BSE is decentralized & the managing teams of the exchange consist of a panel of directors. The board members of this stock company *include various representatives of trading organizations and other professionals headed by the Managing Director. They take part in the formation of programs, policies, and guidelines to control the entire process of the exchange. Apparently, there are 417 cities and several towns that lie within the fold of BSE. During the year FY 04-05 BSE experienced a phenomenal growth which turned out to be fruitful.*

National Stock Exchange of India (NSE)

National Stock Exchange of India

- *Created December 9, 2017*
- *Author Harsh Singh*
- *Category Market Eco System*
- *Comments 2*

NSE, or the National Stock Exchange of India Limited, is India's leading stock exchange. Established in 1992 and located in Mumbai, this exchange brought a paradigm shift to the Indian financial market right after it had suffered a setback due to an unprecedented scam that hit the Bombay Stock Exchange. This article, divided into 4 major sections highlighted below, will introduce you to the legacy of NSE.

History of National Stock Exchange of India

After the outbreak of 1992 security scam in which a BSE member, Harshad Mehta, was exposed manipulating the market, the government of India decided to promote establishing NSE based on recommendations made by High Powered Study Group on Establishment of New Stock Exchanges. The immediate aim was to provide equal access to investors from all across the nation and make participating in stock market easier.

In November 1992, NSE was established as a tax-paying company with key investors including Life Insurance Corporation of India, State Bank of India, IFCI Limited, IDFC Limited and Stock Holding Corporation of India Limited. It was recognized as a stock exchange under the Securities Contracts (Regulation) Act, 1956 in April 1993 and commenced operations in the Wholesale Debt Market (WDM) segment in June 1994. Operations in the *equity segment were started in November 1994 followed by Derivatives segment in June 2000.*

NSE was the first stock exchange in India where ownership, management and trading were handled by three independent set of people. While the ownership is with various financial institutions and banks, the management is handled by independent professionals who are forbidden from directly or indirectly trading on the exchange. This demutualization has eliminated the kind of conflict of interest that was at the root of 1992 security scam.

Functions of NSE

The NSE was set-up with an express objective to fulfil the following functions:

- *establishing a nation-wide trading facility for equities, debt and other hybrid instruments*
- *ensuring equal access to investors across the nation through an appropriate communication network*
- *providing a fair, efficient and transparent securities market to investors using electronic trading systems*
- *enabling shorter settlement cycles and book entry settlements systems, and*
- *meeting the current international standards of securities markets*

*NSE successfully fulfilled these functions by establishing the first electronic stock market of the nation. NSE was instrumental in creating **National Securities Depository Limited** (NSDL), the first depository in India, allowing investors to hold and trade securities electronically. This not only made investing simple, but also provided increased transparency. The price information that was earlier available only to a handful of traders present at the exchange, was now widely* *broadcasted and available to everyone at their own remote location.*

Before the system introduced by NSE, an investor who wanted to trade a security not listed on the nearest exchange had to route orders through a series of correspondent brokers to the appropriate exchange. This resulted in increased uncertainty and high transaction costs. NSE made it possible for an investor to access the same market and order book, irrespective of location and at the same cost as every other investor. NSE trading terminals are now present in 363 cities and towns across India and can be accessed through brokers from anywhere on the globe.

Features of National Stock Exchange

NSE, like every other leading stock exchange today, runs an order-driven market as opposed to quote-driven market. The fully automated screen based trading system that it runs is called ***National Exchange for Automated Trading (NEAT)****.*

The ***order management*** *system under NEAT gives a unique number to each order received and if a match is not found immediately, it is added to an order book where the sequence of orders to be matched are determined based on price-time priority. That is, if two orders are entered into the system, the order having the best price gets the higher priority and within the orders of the same price priority is given to the older order.*

Order matching *is done by comparing the best buy order, the buy order with the highest price, with the best sell order, the sell order with the lowest price. This is because a seller would like to sell to the buyer offering the highest price and vice versa. While orders can be partially matched till the complete order can be completed, the matches are always made based on the passive price of the order and not the active price at which the match is made.*

Demat Account

Demat Account is an account that is used to hold shares and securities in electronic format. The full form of Demat account is a dematerialised account. The purpose of opening a Demat account is to hold shares that have been bought or dematerialised (converted from physical to electronic shares), thus making share trading easy for the users during online trading.

In India, Free Demat account service is provided by depositories such as NSDL and CDSL through intermediaries / Depository Participant / Stock Broker such as Angel Broking. The charges of Demat account vary as per the volume held in the account, type subscribed, and the terms and conditions laid by the depository and the stock broker.

What is Book Building?

Book building is the process by which an underwriter attempts to determine the price at which an initial public offering (IPO) will be offered. An underwriter, normally an investment bank, builds a book by inviting institutional investors (fund managers et al.) to submit bids for the number of shares and the price(s) they would be willing to pay for them.

Understanding Book Building

Book building has surpassed the 'fixed pricing' method, where the price is set prior to investor participation, to become the de facto mechanism by which companies price their IPOs. The process of price discovery involves generating and recording investor demand for shares before arriving at an issue price that will satisfy both the company offering the IPO and the market. It is highly recommended by all the major stock exchanges as the most efficient way to price securities.

MUTUAL FUNDS

Mutual funds have become a hot favourite of millions of people all over the world. The driving force of mutual funds is the 'safety of the principal' guaranteed, plus the added advantage of capital appreciation together with the income earned in the form of interest or dividend. People prefer mutual funds to bank deposits, life insurance and even bonds because with a little money, they can get into the investment game.

What is Mutual Fund

To state in simple words, a mutual fund collects the savings from small investors, invest them in Government and other corporate securities and earn income through interest and dividends, besides capital gain.

IMPORTENCE OF MUTUAL FUNDS

(i) ***DIVERSIFICATION:***

A large number of investors have small savings with them. They can at the most buy shares of one or two companies. When small savings are pooled and entrusted to mutual funds then these can be used to buy shares of many different companies. Thus, investors can participate in a large basket of shares of different companies.

(ii) ***Liquidity***

A peculiar advantage of a mutual fund is that investment made in its schemes Can be converted back into cash promptly without heavy expenditure on brokerage, delays, etc. According to the regulations of SEBI, a mutual fund in India is required to ensure liquidity. For open ended schemes, the investor can always approach the Mutual Fund to repurchase units at declared het assets value ' (NAV). In case of close can easily be sold in the stock market. ended schemes, units *(iii) **Reduced Risk**.*

As mutual funds invest in large number of companies and are managed professionally, the risk factor of the investor is reduced. A small investor, on the other hand, may not be in a position to minimise such risks.

*(iv) **Tax advantage**. There are certain schemes of mutual funds which provide lax advantage under the Income Tax Act. Thus, the tax liability of an investor is also reduced when he invests in these schemes of the mutual funds.*

*(v) **Low Operating costs**.*

Mutual funds have large investible funds at their disposal and thus can avail economics of large scale. This reduces their operating costs by way of brokerage, fees, commission etc. Thus, a small investor also gets the benefit of large scale economies and low operating costs.

*(vi) **Flexibility**.*

Mutual funds provide flexible investment plans to its subscribers such as, regular investment plans, regular withdrawal plans and dividend reinvestment plans, etc. Thus, an investor can invest or withdraw funds according to his own requirements,

*(vii) **Higher Returns**.*

Mutual funds are expected to provide higher return to the investors as compared to direct investment because of professional management, economies of scale, reduced risk, etc.

*(viii) **Investor Protection**.*

Mutual funds are regulated and monitored by the Securities and Exchange Board of India (SEBI). The SEBI Mutual Funds) Regulations, 1996 which have replaced the regulations of 1993, provide better protection to the investors, impart a greater degree of flexibility and facilitate competition

TYPES OF MUTUAL FUNDS

(A) Close - ended Funds

Under this scheme, the corpus of the fund and its duration are prefixed. In other words, the corpus of the fund and the number of units are determined in advance. Once the subscription reaches the pre - determined level, the entry of investors is closed. After the expiry of the fixed period, the entire corpus is disinvested and the proceeds are distributed to the various unit holders in proportion to their holding. Thus, the fund ceases to be a fund, after the final distribution.

Features: *The main features of the close - ended funds are:*

(i) The period and/ or the target amount of the fund is definite and fixed beforehand.

(ii) Once the period is over and/ or the target is reached, the door is closed for the investors. They cannot purchase any more units.

(iii) These units are publicly traded through stock exchange and generally, there is no repurchase facility by the fund.

(iv) The main objective of this fund is capital appreciation.

(B) Open - ended Funds

It is just the opposite of close - ended funds. Under this scheme, the size of the fund and/ or the period of the fund is not pre - determined. The investors are free to buy and sell any number of units at any point of time. Anybody can buy this unit at any time and sell it also at any time at his discretion.

The Main Features of the Open - Ended Funds are:

(i) There is complete flexibility with regard to one's investment or disinvestment. In other words, there is free entry and exit of investors in an open - ended fund. There is no time limit. The investor can join in and come

out from the Fund as and when he desires.

(ii) These units are not publicly traded but, the Fund is ready to repurchase them and resell them at any time.

(iii) The investor is offered instant liquidity in the sense that the units can be sold on any working day to the Fund.

(iv) The main objective of this fund is income generation. The investors get dividend, rights or bonuses as rewards for their investment.

(v) Since the units are not listed on the stock market, their prices are linked to the Net Asset Value (NAV) of the units. The NAV is determined by the Fund and it varies from time to time.

On the Basis of Income

A) Income Funds: *As the very name suggests, this Fund aims at Generating and distributing regular income to the members on a return is higher than periodical basis. It concentrates more on the distribution that of income and it also sees that the average the income from bank deposits.*

The main features of the Income Funds are

(i) The investor is assured of regular income at periodic intervals. say half - yearly or yearly and so on.

(ii) The main objective of this type of Fund is to declare regular dividends and not capital appreciation.

(iii) The pattern of investment is oriented towards high and fixed income yielding securities like debentures, bonds etc.

(iv) This is best suited to the old and retired people who may not have any regular income.

(v) Il concerns itself with short run gains only.

(B) Pure Growth Funds (Growth Oriented Funds)*. Unlike the Income*

Funds, Growth Funds concentrate mainly on long run gains i.e. capital appreciation. They do not offer regular income and they aim at capital appreciation in the long run. Hence, they have been described as " Nest Eggs " investments.

The Main features of the Growth Funds are*.*

(i) The growth oriented Fund aims at meeting the investors ' need for capital appreciation.

(ii) The investment strategy therefore, conforms to the Fund objective by investing the funds predominantly on equities with high growth potential.

(iii) The Fund tries to get capital appreciation by taking much risks and investing on risk bearing equities and high growth equity shares.

(iv) The fund may declare dividend, but its principal objective is only capital appreciation.

(v) This is best suited to salaried and business people who have high risk bearing capacity and ability to defer liquidity. They can accumulate wealth for future needs.

(C) Balanced Funds: *This is otherwise called " income - cum - growth " fund/. It is nothing but a combination of both income and growth funds. It aims at distributing regular income as well as capital appreciation This is achieved by balancing the investments between the high growth equity shares and also the fixed income earning securities.*

(D) Specialised Funds: *These funds invest in a particular type of securities, these funds may specialise in securities of companies dealing in a* *particular product, firms in a particular industry or of certain income producing securities. Ant investor wanting to invest in a particular security will prefer a fund dealing in such securities.*

(E) Money - Market Mutual Funds (MMMFs): *These funds are basically open ended mutual Funds and as such they have all the features of the Open ended Fund. But, they invest in highly liquid and safe securities like commercial paper, banker ' s acceptances, certificates of deposits, Treasury bills etc. These instruments are called money market instruments. They take the place of shares, debentures and bonds in a capital market. They pay money market rates of interest.*

(F) Taxation Funds: *A taxation fund is basically a growth oriented fund. But, it offers tax rebates to the investors either in the domestic or foreign capital market. It is suitable to salaried people who want to enjoy tax rebates particularly during the month of February and March In India, at present the law relating to tax rebates is covered under Sec. 88 of the Income Tax Act, 1961. An investor is entitled to get 20 % rebate in Income Tax for investments made under this fund subject to a maximum investment of Rs. 10, 000/ - per annum.*

OTHER CLASSIFICATION

(G) ***Leveraged Funds:*** *These funds are also called borrowed funds since they are used primarily to increase the size of the value of portfolio of a mutual fund. When the value increases, the earning capacity of the fund also increases. The gains are distributed to the unit holders, This is resorted to only when the gains from the borrowed funds are more than the cost of borrowed funds.*

(H) Dual Funds*: This is a special kind of closed end fund. It provides a single investment opportunity for two different types of investors. For this purpose, it sells two types of investment stocks viz., income shares and capital shares. Those investors who seek current investment income can* *purchase income shares. They receive all the interest and dividends earned from the entire investment portfolio. However, they are guaranteed a minimum annual dividend payment. The holders of capital shares receive all the capital gains earned on those shares and they are not entitled to receive any dividend of any type. In this respect, the dual fund is different from a balanced fund.*

(I) Index Funds: *Index funds refer to those funds where the portfolios are designed in such a way that they reflect the composition of some broad based market index. This is done by holding securities in the same proportion as the index itself. The value of these index linked funds will automatically go up whenever the market index goes up and vice versa.*

(J) Bond Funds: *These funds have portfolios consisting mainly of fixed income securities like bonds. The main thrust of these funds is mostly on income rather than capital gains. They differ from income funds in the sense income funds offer an average returns higher than that from bank deposits and also capital gains lesser than in equity shares.*

VENTURE CAPITAL

CONCEPT OF VENTURE CAPITAL

The term ' Venture Capital ' is understood in many ways. In a narrow sense, if refers to investment in new and tried enterprises that that are lacking a stable record of growth.

In a broader sense, venture capital refers to the commitment of capital as shareholding, for the formulation and setting up of small firm specialising in new ideas or new technologies. It is not merely an injection of funds into a new firm, it is a simultaneous input of skill needed to set up the firm, design its marketing strategy and organise and manage it. It is an association with successive stages of firm ' s development with distinctive types of financing appropriate to each stage of development.

Meaning of Venture Capital

Venture capital is long term risk capital to finance high technology projects which involve risk but at the same time has strong potential for growth. Venture capitalist pool their resources including managerial abilities to assist new entrepreneurs in the Early years of the project. Once the project reaches the stage of profitability, they sell their equity holdings at high premium.

Definition of a Venture Capital Company

A venture capital company is defined as " a financing institution which joins an entrepreneur as a co - promoter in a project and shares the risks and rewards of the enterprise. "

Features of Venture Capital

Some of the features of venture capital financing are as under:

1. *Venture capital is usually in the form of an **equity participation**. It may also take the form of convertible debt or long term loan.*

2. *Investment is made not only in **high risk** but also in high growth potential projects.*

3. *Venture capital is available only for **commercialisation of new ideas** or new technologies and not for enterprises which are engaged in trading, booking, financial services, agency, liaison work or research and development.*

4. ***Venture capitalist** joins the entrepreneur as a co - promoter in projects and share the risks and rewards of the enterprise.*

5. *There is **continuous involvement** in business after making an investment by the investor.*

6. *Once the venture has reached the full potential the venture capitalist*

*disinvests his holdings either to the promoters or in the market. The basic objective of investment is not profit but **capital appreciation** at the time of disinvestment.*

SCOPE OF VENTURE CAPITAL/ STAGES/TYPES OF VENTURE CAPITAL

Venture capital may take various forms at different stages of the project. There are four successive stages of development of a project viz.

Development of a project idea, Implementation of the idea, commercial production and marketing and finally large scale investment to exploit the economics of scale and achieve stability. Financial institutions and banks usually start financing the project only at the second and third stage but rarely from the first stage. But venture capitalist provide finance even from the first stage of idea formulation.

The various stages in the financing of Venture Capital are described below:

*1. **Development Of An Idea- Seed Finance***

In the initial stage venture capitalist provide seed capital for translating an idea into business proposition. At this stage investigation is made indepth which normally takes a year or more.

*2. **Implementation Stage - Start up Finance**:*

When the firm is set up to manufacture a product or provide a service, start up finance is provided by the venture capitalists. The first and second stage capital is used for full scale manufacturing and further business growth.

*3. **Fledging Stage - Additional Finance**:*

In the third stage firm has made some headway and entered the stage of manufacturing product but faces teething problems. It may not be able to generate adequate funds and so additional round of financing is provided to develop the marketing infrastructure.

*4. **Establishment Stage. Establishment Finance:***

At this stage the firm is established in the market and expected to expand at a rapid pace. It needs further financing for expansion and diversification so that is can reap economics of scale and attain stability. At the end of the establishment stage, the firm is listed on the stock exchange and at this point the venture capitalist disinvests their shareholdings through available exist routes.

LEASING

INTRODUCTION

The main objective of a business is to maximise the owner ' s economic welfare. The firm makes investments to maximise stockholder's wealth. After identifying attractive projects, the firm considers various methods of financing them. In addition to debt and equity financing, leasing has emerged as a third important source of intermediate and long - term financing of corporate enterprises during the recent few decades. It is widely used in western countries to finance investments. Prior to 1950, leasing was primarily concerned with real estate, i. c. land and buildings. But today, almost all types of fixed assets can be leased. In India, leasing is a recent development and equipment leasing was introduced by First Leasing Company of India Limited in 1973 only. Since then, a number of medium to large - sized companies, financial institutions like ICICI, IRCI, SICOM and CIC have also entered the field of leasing.

MEANING

Leasing is an arrangement that provides a firm with the use and control over assets without buying and owning the same. It is a form of renting assets. Lease is a contract between the owner of the asset (lessor) and the *user of the asset called the lesser, whereby the lessor gives the right to use the asset to the lessee over an agreed period of time for a consideration called the lease rental. The lease contract is regulated by the terms and conditions of the agreement. The lessee pays the lease Tent periodically to the lessor as regular fixed payments over a period of time. The rentals may be payable at the beginning or end of a monthly, quarter, half - year or year. The lease rentals can also be agreed both in terms of amount and timing as per the profits and cash flow position of the lessee. At the expiry of the lease period, the asset reverts back to the lessor who is the legal owner of the asset.*

ESSENTIAL ELEMENTS OF LEASING

*1. **No. of Parties to the Contract.** There are always two parties to a contract of lease financing*

(a) The user or the lessee *(b) The owner or the lessor*

*2. **Asset.** The subject matter of a lease financing contract may be an asset, property equipment e.g. plant and machinery, land and building etc.*

*3. **Consideration.** The right to use an asset is given to lessee for a consideration called lease rental. Lease rent is determined by the lessor taking into consideration the capital invested in the asset, depreciation, interest on capital, repairs etc.*

*4. **Lease Period.** A contract of leasing is usually undertaken for a fixed period (no. of years). It may sometimes spread over the entire economic/ useful life of the asset. At the expiry of the lease period, the asset reverts back to the lesser who is the legal owner of the asset.*

*5. **Use VIS. Ownership.** During the term of lease, ownership of the asset* *remains with the lessor where as the possession of asset lies with the lessee. He is allowed to use the asset during the tenure of lease agreement.*

Types of Leasing

1. ***Operating Leasing***
2. ***Financial Leasing***

OPERATING OR SERVICE LEASE

An operating lease is usually characterised by the following features:

(i) It is a short - term lease on a period to period basis. The lease period in such a contract is less than the useful life of the asset.

(ii) The lease is usually cancellable at short - notice by the lessee.

(iii) As the period of an operating lease is less than the useful life of the asset, it does not necessarily amortize the original cost of the asset. The lessor has to make further leases or sell the asset to recover his cost of investment and expected rate of return.

(iv) The lessee usually has the option of renewing the lease after the expiry of lease period.

(v) The lessor is generally responsible for maintenance, insurance and taxes of the asset. He may also provide other services to the lessee.

As it is a short - term cancellable lease, it implies higher risk to the lessor but higher lease rentals to the lessee Operating or service leasing is common to the equipment which require expert technical stat for maintenance and are exposed to technological developments, e.g. computers, vehicles

II. FINANCIAL LEASE

A lease is classified as financial lease if it ensures the term of the lessor for amortisation of the entire cost of investment plus the expected return on capital outlay during the term of the lease. Such a lease is usually for a longer period and non - cancellable. As a source of funds, the financial leases is an alternative similar to debt financing. Most of the leases in India are financial leases that are commonly used for leasing land, building, machinery and fixed equipment.

A financial lease is usually characterised by the following features*:*

(1) The present value of the total lease rentals payable during the period of the lease exceeds or is equal to substantially the whole of the fair value of the leased asset. It implies that within the lease period, the lessor recovery his investment in the asset along with an acceptable rate of return.

(2) As compared to operating lease, a financial lease is for a longer period of time.

(3) It is usually non - cancellable by the lessee prior to its expiration date.

(4) The lessee is generally responsible for the maintenance, insurance and service of the asset. However, the terms of lease agreement, in some cases. may require the lessor to maintain and service the asset. Such an arrangement is called ' ***Maintenance or gross lease'****.*

(5) A financial lease usually provides the lessee an option of renewing the lease for further period at a nominal rent.

Forms of Financial Lease arrangements:

The following are the important forms of financial lease arrangements:

*(i) **Sale and Leaseback**. A sale and leaseback arrangement involves the sale of an asset already owned by a firm (vendor) and leasing of the same asset back to the vendor from the buyer.*

This form of lease arrangement enables a firm to receive cash from the sale of asset and also retain the economic use of the asset in consideration of periodic lease payments. A sale and leaseback arrangement is generally preferred by firms facing shortage of working capital funds. The lessors engaged in sale and lease back include insurance companies, pension funds, private finance companies and financial institutions.

*(ii) **Direct Leasing**. In contrast with sale and leaseback, under direct leasing a firm acquires the use of an asset that it does not already man. A direct lease may be arranged either the manufacturer supplier directly or through the leasing company.*

In the first case, the manufacturer/ supplier himself acts as the lessor while in the second case the lessee firm arranges the purchase of the asset for the leasing company (lessor) from the manufacturer or the supplier and also enters into an agreement with the lessor for the lease of on the asset.

*(iii) **Leveraged Lease**. A leveraged lease is an arrangement under which the lessor borrows funds for purchasing the asset, from a third party called lender which is usually a bank, finance company. The loan is usually secured by the mortgage of the asset and the lease rentals to be received from the lessee. The loan is paid back out of the lease rentals, may be directly by the lessee by paying only the excess amounts to the lessor. The lessor acts as the owner as well as the borrower and the lender is usually a bank insurance company financial institution or a private financing*

company.

*(iv) **Straight Lease and Modified Lease**. Straight lease requires the lessee firm to pay lease rentals over the expected service life of the asset and does not provide for any modifications to the terms and conditions of the basic lease.*

Modified lease, on the other hand, provides several options to the lessee during the lease period. For example, the option of terminating the lease may be provided by either purchasing the asset or returning the same.

*(v) **Primary and Secondary Lease (Front - ended and Back - ended Lease)**. Under primary and secondary lease, the lease rentals are charged in such a manner that the lesser recovers the cost of the asset and acceptable profit during the initial period of the lease and then a secondary lease is provided at nominal rentals. In simple words, the rentals charged in the primary period are much more than that of the secondary period. This form of lease arrangement is also known as front - ended and back - ended lease.*

OTHER TYPES OF LEASES

***(1) Floating Rental Rate Lease Contracts**. Frequent changes in the interest rates in the last few years have led to this type of lease contract. Under this type of lease, lease rentals are reduced or increased according to the borrowing rates by the lessor. This type of lease contract permits the lessee to undertake the risk and enjoy the benefits of interest rate variations*

***(2) Domestic Lease and International Lease**. When the lessor, lessee and the equipment supplier involved in the lease contract are resident in the same country, the lease transaction is said to be domestic lease. When the parties to the lease contract are residing in different countries it is known as international lease.*

It is of two types:

(a) ***Import Lease***. *In this type of lease, both the lessor and lessee are residing in the same country but the equipment supplier belongs to different country. The lessor first imports the equipment and leases it to the lessee.*

(b) ***Cross Border Lease***. *When a lessor - leases an equipment to a lessee who is not falling in the jurisdiction of the lessor ' s country then the lease is known as cross Border leasing, the domicile of the supplier is immaterial.*

(3) Sale - Aid Leasing. *Under this type of leasing, a manufacturer directly extends facility of leasing either by one of his own subsidiaries of through a third party. The leasing enables a manufacturer to have direct liaison with the customer, ensure regular updating or replacement of equipment and improve sales position. The lessee is also at great advantage because he gels asset on monthly payment basis spread out on a very long period. He gets the asset installed and operational without incurring capital expenditure.*

MERCHANT BANKING

Introduction

The term merchant banking is used differently in different countries and so there is no precise definition for it, In London, merchant banker refers to those who are members of British Merchant Banking and Securities House Association who carry on consultation, leasing, portfolio services, assets management, euro credit, loan syndication etc. In America, merchant banking is concerned with mobilising savings of people and directing the funds to business enterprise.

Definition

There is no universal definition for merchant banking. It assumes diverse functions in different countries. So merchant banking may be defined as, ' an institution which covers a wide range of activities such as management of customer services, portfolio management, credit syndication, acceptance credit, counselling, insurance etc.

The Notification of the Ministry of Finance defines a merchant banker as, " any person who is engaged in the business of issue management either by making arrangements regarding selling, buying or subscribing to the securities as manager, consultant, adviser or rendering corporate advisory service in relation to such issue management ".

MERCHANT BANKING IN INDIA

In India prior to the enactment of Indian Companies Act, 1956 managing agents acted as issue houses for securities, evaluated project reports, planned capital structure and to some extent provided venture capital for new firms. Few share broking firms also functioned merchant bankers.

The need for specialised merchant banking service was felt in India with the rapid growth in the number and size of the issues made in the primary market. The merchant banking services were started by foreign banks, namely the National Grindlays Bank in 1967 and the City Bank *in 1970. The Banking Commission in its report in 1972 recommended the setting up of merchant banking institutions by commercial banks and financial institutions. This marked the beginning of specialised merchant banking in India. To begin with, merchant banking services were offered along with other traditional banking services. In the mid - eighties, the Banking Regulations Act was amended permitting commercial banks to offer a*

wide range of financial services through the subsidiary rule. The State Bank of India was the first Indian Bank to set up Merchant Banking Division in 1972. Later ICICI set up its Merchant Banking Division followed by Bank of India, Bank of Baroda, Canara Bank, Punjab National Bank and UCO Bank. The merchant banking gained prominence during 1983 - 84 due to new issue boom.

MERCHANT BANKS AND COMMERCIAL BANKS TV

There are differences in approach, attitude and areas of operations between commercial banks and merchant banks. The differences between merchant banks and commercial banks are summarised below:

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

2. Commercial banks are asset oriented and their lending decisions are based on detailed credit analysis of loan proposals and the value of security offer against loans. They generally avoid risks.

SCOPE FOR MERCHANT BANKING IN INDIA

In the present day capital market scenario, the merchant banks play the role of an encouraging and supporting force to the entrepreneurs, corporate sectors and the investors. There is vast scope for merchant bankers to enlarge their operations both in domestic and international market.

1. ***Growth of New Issues Market*** -

The growth of new issue market is unprecedented since 1990 amount of annual average of capital issues by non - government public companies was only about 90 crores in the 70s, the same rose to over Rs. 1, 000 ers in the 80s ' and further to Rs. 12, 700 crores in the first four years of 1990 ' s. This figure could be well beyond Rs. 40, 000 crores by the end of 1994 - 95. The number of capital issues has also increased from 363 in 1990 - 91 to 900 in 1993 - 94. The trend is expected to continue in future.

2. ***Entry of Foreign Investors***

An outstanding development in the history of Indian capital market was its opening up in 1992 by allowing foreign institutional investors to invest in primary and secondary market and also permitting Indian companies to directly tap foreign capital through euro issues. Within two years to March 1994, the total inflow of foreign capital through these routes reached to about $ 5 billion. It is estimated that this figure may go up to $ 35 - 40 billion by the turn of this century.

3. ***Changing Policy of Financial Institutions***

With the changing emphasis in the lending policies of financial institutions from security orientation to project orientation, corporate enterprises would *require the expert services of merchant bankers from project appraisal, financial management etc. The policy of decentralization and encouragement of small and medium industries will further increase the demand for technical and financial services which can be provided by merchant bankers.*

*4. **Development of Debt Market***

The concept of debt market has set to work through National Stock Exchange and the Over the Counter Exchange of India. Experts feel that of the estimated capital issues of Rs. 40, 000 crores in 1994 - 95, a good portion may be raised through debt instruments. The development of debt market will offer tremendous opportunity to Merchant Bankers.

*5. **Innovations in Financial Instruments***

The Indian capital market has witnessed innovations in the introduction of financial instruments such as non - convertible debentures with detachable warrants, cumulative convertible preference shares, zero coupon bonds, deep discount bonds, triple option bonds, secured premium notes, floating rate bonds, auction rated debentures etc. This has further extended the role of Merchant Bankers as market makers for these instruments.

*6. **Corporate Restructuring***

As a result of liberalisation and globalisation the competition in the corporate sector is becoming intense. To survive in the competition, companies are reviewing their strategies, structure and functioning. This had led to corporate restructuring including mergers, acquisitions, splits, disinvestments and financial restructuring. This offers good opportunity to Merchant Bankers to extend the area of their operations.

*7. **Disinvestment***

The government raised Rs. 2000 crores through disinvestment of equity shares of selected public sector undertakings in 1993 - 94. The government *proposes to shift the present method of periodic sale of public sector shares to round the year off loading of shares directly on the stock exchange from the year 1995 - 96. The government will sell the shares of identified public sector at any time during the year when they get a good price above minimum stipulated level. This is likely to provide good business to Merchant Bankers in future.*

The above discussion highlights, that the scope of merchant banking

is vast and there lies immense opportunities ahead of Merchant Bankers

SERVICES OF MERCHANT BANKS

The financial institutions in India could not meet the demand for long term funds required by the ever expanding industry and trade. corporate sector enterprises, therefore, meet their requirements ach issue of shares and debentures in the capital market. To raise money from capital market, promoters bank upon merchant bankers manage the whole show by rendering multifarious services. The merchant bankers also advise the investors of the incentives available in the form of tax reliefs and other statutory obligations,

The services of merchant bankers are described in detail in the following section :

(i) ***Corporate Counselling***

Corporate counselling covers the entire field of merchant banking activities viz. project counselling, capital restructuring, project management, public issue management, loan syndication, working capital, fixed deposit, lease financing, acceptance credit etc. The scope of corporate counselling is limited to giving suggestions and opinions *to the client and help taking actions to solve their problems. It is provided to a corporate unit with a view to ensure better performance, maintain steady growth and create better image among investors*

(ii) ***Project Counselling***

Project counselling includes preparation of project reports, deciding upon the financing pattern to finance the cost of the project and appraising project report with the financial institutions or banks. Project reports are prepared to obtain government approval, get financial assistance from institutions and plan for the public issue. The financing mix is to be decided keeping in view the rules, regulations and norms prescribed by the government or followed by financial institutions. The projects are appraised, as to the location, technical, commercial and financial viability of the project. Project counselling

ii) Loan Syndication

Loan syndication refers to assistance rendered by merchant banks to get mainly term loans for projects. Such loans may be obtained from a single development finance institution or a syndicate or consortium. Merchant Bankers help corporate clients to raise syndicated loans from commercial banks. Merchant Banks help clients approach financial institutions for term loans. The decision as to which financial institution should be approached depends on industry, location of the unit and size of project cost.

The Merchant Bankers, first, make an appraisal of the project to satisfy that it is viable. The next step is designing capital structure. determining the promoter ' s contribution and arriving at a figure of approximate amount of term loan to be raised. The Merchant Banker has to ensure that the project adheres to the guidelines for financing industrial projects. After verifications that the project would be eligible for term loan, a preliminary meeting is fixed with financial institution. If the financial institution agrees to consider the proposal, the application is filled in and submitted along with other documents. The Merchant Bankers involvement enables the *company to state that it has exercised due diligence in the exercise of obligations under variousregulations.*

(iv) ***Issue Management***

Management of issue involves marketing of corporate securities viz., equity shares, preference shares and debentures or bonds by offering them to public. Merchant banks act as intermediary whose main job is to transfer capital from those who own it to those who need it. The issue function may be broadly dividend into pre – issue management and post issue management. In both the stages, legal requirements have to be complied with and several activities connected with the issue have to be co - ordinated.

The pre - issue management is divided into:

(i) Issue through prospectus, offer for sale and private placement.

(ii) Marketing and underwriting. *(iii) Pricing of Issues,*

(v) ***Underwriting of Public Issue***

Underwriting is a guarantee given by the underwriter that in the event of under subscription the amount underwritten, would be subscribed by him. It is an insurance to the company which proposes to make public offer against risk of under subscription. The issues packed by well-known underwriters generally receive a high premium from the public. This enables the issuing company to sell securities quickly.

(vi) ***Managers, Consultants or Advisers to the Issue***

The managers to the issue assist in the drafting of prospectus, application forms and completion of formalities under the Companies Act, appointment of Registrar for dealing with share applications and transfer and listing of shares of the company on the stock exchange.

Companies are free to appoint one or more agencies as managers to the *issue. SEBI guidelines insist that all issues should be managed by atleast one authorized merchant banker. Ordinarily, not more than two merchant bankers should be associated as lead managers, advisers and consultants to a public issue. In issues of over Rs. 100 crores, upto a maximum of four merchant bankers could be associated as managers.*

*(vii) **Portfolio Management***

Portfolio refers to investment in different kinds of securities such as shares, debentures or bonds issued by different companies and securities issued by the government. It is not merely a collection of unrelated assets but a carefully blended asset combination within a unified framework. Portfolio management refers to maintaining proper combination of securities in a manner that they give maximum return with minimum risk.

PROBLEMS OF MERCHATN BANKING

1. *SEBI guidelines have authorized merchant bankers to undertake issue related activities only with an exception of portfolio management. These guidelines have made the merchant bankers either to restrict their activities or think of separating these activities from the present one and float new subsidiary and enlarge the scope of its activities.*
2. *SEBI guidelines stipulate a minimum net worth of Rs. 1 crore for authorisation of merchant bankers. Small but professional and specialised merchant bankers who do not have a net worth of Rs. 1 crore may have to close down their business. The entry is denied to young, specialised professionals into merchant banking business.*
3. *Non co - operation of the issuing companies in timely allotment of securities and refund of application money is another problem of merchant*

bankers. The guidelines have put the responsibility on the merchant bankers. They have to seek the co - operation of the issuing company to shoulder the responsibility