Money Market and Capital Market in India: Instruments and Details
Part-1

Money market can be defined as a market for short-term funds with maturities ranging from overnight to one year and includes financial instruments that are considered to be close substitutes of money. Money market transactions could be both secured and unsecured, i.e., without collaterals as we will see ahead.

Money market covers sources of finance - lending and borrowing short term funds- funds with a maturity of less than one year. Banks and financial institutions(IDBI, LIC etc) individuals, mutual funds, companies and government are the main lenders and borrowers. The informal market operates through small-scale money-lenders as well as others outside the RBI control.

Money market instruments broadly are: call money; bill market (both commercial bills and treasury bills) Certificates of Deposit(CD); Commercial paper(CP).

Call Money

Call/Notice money is money borrowed or lent for a very short period. If the period is more than one day and up to 14 days it is called 'Notice money' otherwise the amount is known as Call money'. No collateral security is required to cover these transactions and good will and reputation are the basis apart from the documents like promissory notes. The call market enables the banks and institutions to even out their day to day deficits and surpluses of money.

Commercial banks, Co-operative Banks, mutual funds, primary dealers and others are allowed to borrow and lend in this market Interest rates in the call and notice money market are market determined. A **primary dealer** is a firm that buys government securities directly from a government, with the intention of reselling them to others, thus acting as a market maker of government securities. The government may regulate the behavior and numbers of Its primary dealers and impose conditions of entry.

Treasury Bills

Treasury bills are short-term money market instruments, which are issued by the RBI on behalf of the GOI. The GOI uses these funds to meet its short-term financial requirements of the government. T-Bills are sovereign zero risk instruments. They are available in primary and secondary market; issued at a discount to face value i.e., investors may buy the T-bill at discount to face value of Rs.100 and on maturity the face value of Rs.100 is received by the investor.

Treasury bills (T-bills) offer short-term investment opportunities. They are thus useful in managing short-term liquidity. At present, the Government of India, through the RBI, issues three types of treasury bills through auctions, namely, 91-day, 182-day and 364-day. There are no treasury bills issued by State Governments.
Treasury bills are also issued under the Market Stabilization Scheme (MSS).

While 91-day T-bills are auctioned every week on Wednesdays, 182-day and 364-day T-bills are auctioned every alternate week on Wednesdays.
Treasury bills are available for a minimum amount of Rs.25,000 and in multiples of Rs. 25,000. Treasury bills are issued at a discount and are redeemed at par.
Treasury bills are zero coupon securities and pay no interest. They are issued at a discount and redeemed at the face value at maturity. For example, a 91 day Treasury bill of Rs.100/- (face value) may be issued at say Rs. 98.20, that is, at a discount of say, Rs.1.80 and would be redeemed at the face value of Rs.100/-. The return to the investors is the difference between the maturity value or the face value (that is Rs.100) and the issue price.
A considerable part of the government's borrowings takes place through T bills of various maturities. The usual investors in these instruments are banks, insurance companies and FIs.

Cash Management Bills (CMBs)

Government of India, in consultation with the Reserve Bank of India, has decided to issue a new short-term instrument, known as Cash Management Bills (CMBs), to meet the temporary mismatches in the cash flow of the Government. The CMBs have the generic character of T-bills but are issued for maturities less than 91 days. Like T-bills, they are also issued at a discount and redeemed at face value at maturity.

Inter Bank Term Money

Inter bank market for deposits of maturity beyond 14 days and upto three months is referred to as the term money market.

Certificates Of Deposit

After treasury bills, the next lowest risk category investment option is the certificate of deposit (CD) issued by scheduled commercial banks and FIs. Regional rural banks and Local area banks can not issue CDs.

CD is a negotiable promissory note, secure and short term (up to a year) in nature. A CD is issued at a discount to the face value, the discount rate being negotiated between the issuer and the investor. CDs can be issued by scheduled commercial banks and select all-India Financial Institutions. Minimum amount of a CD should be Rs.1 lakh The maturity period of CDs issued by banks should be not less than 15 days and not more than one year. The FIs can issue CDs for a period not less than 1 year and not exceeding 3 years from the date of issue. CDs can be issued to individuals or firms.

Inter Corporate Deposits Market

Apart from CPs, corporates also have access to another market called the inter corporate deposits (ICD) market. An ICD is an unsecured loan extended by one corporate to another. Existing mainly as an avenue for low rated corporates, this market allows fund- surplus Corporate to lend to other corporates.

Commercial Paper

It represents short term unsecured promissory notes issued by top rated corporates, primary dealers(PDs),satellite dealers(SDs) and the all-India financial institutions(FIs).
CP can be issued for maturities between a minimum of 7 days and a maximum of up to one year from the date of issue. However, the maturity date of the CP should not go beyond the date up to which the credit rating of the issuer is valid.CP can be issued in denominations of Rs.5 lakh or multiples thereof.

The main features of these papers are

- corporates having tangible net worth of not less than Rs.4 crore can issue them
- All CPs require credit rating from a credit rating agency Minimum amount invested by single investor is Rs.five lakh or multiple thereof.
- CPs are issued at a discount to face value.

Ready Forward Contracts (Repos)

See chapter on Monetary policy.

Commercial Bills

Bills of exchange are negotiable instruments drawn by the seller (drawer) of the goods on the buyer (drawee) of the goods for the value of the goods delivered. These bills are called trade bills. These trade bills are called commercial bills when they are accepted by commercial banks. If the bill is payable at a future date and the seller needs money immediately, he may approach his bank for discounting the bill.

Discount and Finance House of India (DFHI)

Set up in 1988 by RBI to strengthen the bill market. It has been established to deal in money market instruments in order to provide liquidity. Thus the task assigned to DFHI is to develop a secondary market in the existing money market instruments.The main objective of DFHI is to facilitate the smoothening of the short term liquidity imbalances by developing an active money market and integrating the various segments of the money market.
At preset DFHI's activities are restricted to:
1. Dealing in Treasury Bills
2. Re-discounting short term commercial bills.
3. Participating in the inert bank call money, notice money and term deposits and
4. Dealing in Commercial Paper and Certificate of deposits.
5. Government dated Securities

Libor

The London Interbank Offered Rate is the average interest rate estimated by leading banks in London that they would be charged if borrowing from other banks. It is usually abbreviated to BBA Libor (for British Bankers' Association Libor). It is the primary benchmark, along with the Euribor, for short term interest rates around the world.

Many financial institutions, mortgage lenders and credit card agencies set their own rates relative to it. At least $350 trillion in derivatives and other financial products are tied to the Libor.

Mibor - Mumbai Inter-Bank Offer Rate

The Committee for the Development of the Debt Market that had studied and recommended the modalities for the development for a benchmark rate for the call money market. Accordingly, NSE had developed and launched the NSE Mumbai Inter-bank Bid Rate (MIBID) and NSE Mumbai Inter-bank Offer Rate (MIBOR) for the overnight money market in 1998. The **MIBID/MIBOR** rate is used as a bench mark rate for majority of deals.

Money market reforms

The recommendations of the Sukhmoy Chakravarty Committee on the Review of the Working of the monetary system, and the Narasimham Committee Report on the Working of the Financial System in India, 1991, The Reserve Bank of India initiated a series of money market reforms basically directed towards the efficient discharge of its objectives.

Reforms made in the Indian Money Market are:- Deregulation of the Interest Rate ; Money Market Mutual Fund (MMMFs) are allowed to sell units to corporate and individuals. The Discount and Finance House of India (DFHI) was set up in April 1988 to impart liquidity in the money market. It was set up jointly by the RBI, Public sector Banks and Financial Institutions. DFHI has played an important role in stabilizing the Indian money market. Liquidity Adjustment Facility (LAF) - Through the LAF, the RBI remains in the money market on a continue basis through the repo transaction. LAF adjusts liquidity in the market through absorption and or injection of financial resources. In order to impart transparency and efficiency in the money market transaction the electronic dealing system has been started. It covers all deals in the money market. Similarly it is useful for the RBI to watchdog the money market. Establishment of the CCIL: The Clearing Corporation of India limited (CCIL) was set up in April 2001. Development of New Market Instruments like CMBs.

Money Market and Capital Market in India: Instruments and Details: Part-2

Capital Market

It refers to market for funds with a maturity of 1 year and above, refered to as term funds that include medium and long term funds. The demand for these funds comes from both the government for its investtment purposes and also the private sector. Banks, public financial institutions like LIC and GIC; development financial institutions like ICICI, IDBI etc; mutual funds like UTI are the main participants in the market.The elements of the capital market in India are the following:

Government securities,industrial securities that include the shares and debentures of Indian companies- both the primary and secondary market(please refer to the section on stock market) DFIs(IFCI, IDBI, State Financial Corporations(SFCs);UTI, ICICI(private sector) Financial intermediaries: merchant banks; mutual funds;leasing companies; venture capital companies;and others.

G-Secs (Gift edged securities)

A Government security is a tradable instrument issued by the Central Government or the State Governments. It acknowledges the Government's debt obligation. Such securities are short term (usually called treasury bills or Cash Management Bills with original maturities of less than one year) or long term (usually called Government bonds or dated securities with original maturity of one year or more). In India, the Central Government issues both, treasury bills and bonds or dated securities while the State Governments issue only bonds or dated securities, which are called the State Development Loans (SDLs). Government securities carry practically no risk of default and, hence, are called risk-free gilt-edged instruments. Government of India also issues savings instruments (Savings Bonds, National Saving Certificates (NSCs), etc.) or special securities (oil bonds, Food Corporation of India bonds, fertiliser bonds, power bonds, etc.). They are, usually not fully tradable and are, therefore, not eligible to be SLR securities.

Dated Government securities are long term securities and carry a fixed or floating coupon (interest rate) which is paid on the face value, payable at fixed time periods (usually half-yearly). The tenor of dated securities can be up to 30 years.

The G-Sec instrument is in the nature of a bond.

GOI Dated Security can be held by any person, firm, company, corporate body or institution, State Governments, Provident Funds and Trusts. Non-Resident Indians (NRIs, viz., Indian citizens and Individuals of Indian origin), Overseas corporate bodies predominantly owned by NRIs and Foreign Institutional Investors registered with SEBI and approved by Reserve

Bank of India are also eligible to invest in the government stock. G-Sec are issued both in demat and physical form.

The minimum investment in G-Secs is Rs 10,000. G-Secs could be of the following types:

Dated Securities: They have fixed maturity and fixed coupon rates payable half yearly and are identified by their year of maturity.

Floating Rate Bonds:

They are bonds with variable interest rates with a fixed percentage over a benchmark rate. There may also be a cap and a floor rate attached, thereby fixing a maximum and minimum interest rate payable on it.

Capital Indexed Bonds: They are bonds where the interest rate is a fixed percentage over the wholesale price index or CPI.

Capital Index Bond (CIB), 2002 was issued in 1997 where only principal repayments at the time of redemption were indexed to inflation. A new version of IIB has been designed with protection from inflation to both interest payments and principal repayments linking them to Wholesale Price Index (WPI) by the RBI and may be issued (2013).

2012 reforms in G-Secs

The existing limit for investment by Securities and Exchange Board of India (SEBI) registered foreign institutional investors (FIIs) in Government securities (G-Secs) has been enhanced to $30 billion.(2013) and it may be further relaxed.

RBI has decided to allow long term investors like Sovereign Wealth Funds (SWFs), multilateral agencies, endowment funds, insurance funds, pension funds and foreign central banks to be registered with SEBI, to also invest in G-Secs.FII debt is rupee debt and so is welcome.

SDL

State Governments also raise loans from the market. SDLs are dated securities issued through an auction similar to the auctions conducted for dated securities issued by the Central Government. Interest is serviced at half-yearly intervals and the principal is repaid on the maturity date. Like dated securities issued by the Central Government, SDLs issued by the State Governments qualify for SLR. They are also eligible as collaterals for borrowing through market repo as well as borrowing by eligible entities from the RBI under the Liquidity Adjustment Facility (LAF).

DFIs or Development Banks

Financial institutions assume a critical role in the provision of long term credit, especially in the absence of a well-developed long-term debt market. The financial institutions could be categorised into three broad heads, viz., all-India financial institutions (AIFIs), state-level institutions and other institutions. Of the three categories, AIFIs are the most dominant in terms of assets and range of operations.

The major AIFIs are the Industrial Development Bank of India (IDBI), IFCI Ltd., Industrial Investment Bank of India Ltd. (IIBI), Small Industries Development Bank of India (SIDBI), National Housing Bank (NHB), National Bank for Agriculture and Rural Development (NABARD), Export Import Bank of India (EXIM Bank), Tourism Finance Corporation of India Ltd. (TFCI), Unit Trust of India (UTI), Life Insurance Corporation of India (LIC), General Insurance Corporation of India (GIC) and its subsidiaries and Infrastructure Development Finance Company of India Ltd. (IDFC). All these institutions operate on all-India basis. Other institutions comprise Export Credit and Guarantee Corporation (ECGC) and Deposit Insurance and Credit Guarantee Corporation (DICGC).

The state level institutions consist of state financial corporations (SFCs) and state industrial development corporations (SIDCs).

Merchant Banks / Investment Banks

MBs are those who manage and underwrite (Underwriting an issue means to guarantee to purchase any shares in a new issue or rights issue not fully subscribed by the public.) new public issues floated by companies to raise funds from public. They advise corporate clients on fund raising. They are also called investment banks (I banks) .They deal only with corporates and not general public, essentially.

Lehman Brothers was a global financial services firm. Before declaring bankruptcy in 2008, Lehman was the fourth-largest investment bank in the US (behind Goldman Sachs, Morgan Stanley, and Merrill Lynch), doing business in investment banking, equity ,trading (especially U.S. Treasury securities), research, investment management, private equity and private banking.

On September 15, 2008, the firm filed for Chapter 11 bankruptcy protection following the massive exodus of most of its clients, drastic losses in its stock, and devaluation of its assets by credit rating agencies.

Collective investment schemes

For the last few years, the Securities Exchange Board of India (Sebi) has been coming down hard on companies running collective investment schemes (CIS). These schemes, much in the news since the Saradha scam(2013), are those in which people invest to create a pool of money which is then utilised to realise some income for the investors, or acquire some produce, or some properties which are then looked after by a manager of behalf of the investors. In other words a property is owned by an individual, but is maintained jointly with the manager. A mutual fund is also called a collective investment scheme. SEBI introduced regulations for CISs in 1999. In 2013, they are further rendered more stringent.

Tightening the controls on entities running illegal collective investment schemes (CIS), in September 2013, the Securities and Exchange Board of India (Sebi) has notified new norms to classify such activities as frauds and impose penalties of up to three times of their profits.

Besides, the new rules expand the list of activities to be covered under fraudulent and unfair trade practices to hold individuals as well as companies equally guilty for manipulations.

The amendments have been made to Sebi's 'prevention of fraudulent and unfair trade practices' (PFUTP) regulations.
In the backdrop of Sahara / Sharada scams, SEBI modified the definition of CIS to include any scheme / arrangment floated by any person (instead of a company as was defined earlier); and any such scheme with corpus of more than Rs. 100 Crore shall also be deemed to be a CIS by SEBI.

Alternative Investment Funds

AIFs is a newly created class of pooled-in investment vehicles for real estate, private equity and hedge funds. The AIFs have been divided into three categories. The Category I AIFs include those investing in start-ups, social ventures, SMEs, infrastructure or other areas that can get government incentives for being 'socially or economically desirable'. The Category II AIFs include private equity funds and debt funds which do not get any incentives or concessions from the government and do not undertake leverage or borrowing other than to meet day-today operational requirements. The Category III includes hedge funds or funds which trade with a view to make short-term returns.
Angels are the new category introduced in September 2013. (Read ahead)
AIFs are basically funds established or incorporated in India for the purpose of pooling in capital from Indian and foreign investors for investing as per a pre-decided policy. Sebi regulates them. it excludes Mutual funds or collective investment Schemes, family trusts, Employee Stock Option etc.

Mutual Funds

Mutual funds raise money from public and invest them in stock market securities; bonds etc.Mutual funds were virtually synonymous with the Unit Trust of India(UTI) till two decades ago when India witnessed financial sector liberalization and many more public sector and private mutual funds came up. SEBI regulates mutual funds.

Hedge fund

Hedge fund is an MF though it is limited to few; non-transparent and is not fully regulated. The investment styles of the HFs are also criticised as they are not safe and aim at fast returns thus creating volatility in the markets. SEBI does not allow them. To sum up and explain: A hedge fund is a pooled investment vehicle administered by a professional management firm. Hedge funds invest in a diverse range of markets and use a wide variety of investment styles and financial instruments.The name "hedge fund" refers to the hedging techniques traditionally used by hedge funds, but hedge funds today do not necessarily hedge. Hedge funds are made available only to certain investors and cannot be offered or sold to the general public. As such, they generally avoid direct regulatory oversight, bypass licensing requirements applicable to investment companies, and operate with greater flexibility than mutual funds and other investment funds. They are a form of AIFs.

Venture Capital

Venture capital is money provided by financial institutions who invest alongside management in young, rapidly growing companies that have the potential to develop into significant economic contributors. Venture capital is an important source of equity for start-up companies.

Angel Investors

An angel investor or angel (also known as a business angel or informal investor) is an affluent individual who provides capital for a business start-up, usually in exchange for convertible debt or ownership equity. They invest their own money unlike a venture capitalist who invests public money. They became popular in recent years after the web-based enterprises came up in the 1990's.
With an aim to encourage entrepreneurship in the country by financing small start-ups, market regulator Sebi in September 2013 notified new norms for angel investors, who provide funding to companies at their initial stages.

Angel investors are allowed to be registered as Alternative Investment Funds (AIFs) -- a newly created class of pooled-in investment vehicles for real estate, private equity and hedge funds.

In order to ensure investment by angel funds is genuine, the Securities and Exchange Board of India (Sebi) has restricted investment by such funds between Rs 50 lakh and Rs 5 crore.

Among other norms included, angel funds can make investments only in those companies which are incorporated in India. These funds need to be invested in a firm for at least three years, can invest in companies not older than 3 years.

Angel funds are required to have a a corpus of at least Rs 10 crore and minimum investment by an investor should be Rs 25 lakh.

The regulator also stipulated that the fund must not have any family connection with the investee company.

The new norms would help in encouraging entrepreneurship in the country by financing small start-ups at a stage where such start-up finds it difficult to obtain funds from traditional sources of funding such as banks, financial institutions among others.

Finance Minister P Chidambaram in his budget speech had announced that Sebi would frame guidelines for angel investor pools by which they can be registered under AIF venture capital funds (VCF).

Under Sebi guidelines, AIFs already have sub-categories such as Venture Capital Funds, Social Funds and SME Funds. Angel fund is likely to be a separate sub-category.

Regarding raising of funds by an individual investor, the person need to have an experience of 10 years and should possess assets of at least Rs 2 crore.

Hundi

Hundis were legal financial instruments that evolved in India. These were used in trade and credit transactions; they were used as remittance instruments for the purpose of transfer of funds from one place to another. In the era of bygone kings and the British Raj these Hundis served as Travellers Cheques. They were also used as credit instruments for borrowing and as bills of exchange for trade transactions.

Technically, a Hundi is an unconditional order in writing made by a person directing another to pay a certain sum of money to a person named in the order. Being a part of an informal system, hundis now have no legal status and were not covered under the Negotiable Instruments Act, 1881. They were mostly used as cheques by indigenous bankers.
Chit funds

Saradha Group run as a collective investment scheme (CIS), which is regulated by the Securities and Exchange Board of India, collapsed and caused severe losses to many people.

There are various such financial schemes such as chit funds, multi-level marketing schemes or ponzi schemes which are all different from one another.

In simple terms, a chit fund is an arrangement that a group of people arrive at to contribute money in a defined manner at periodic intervals into a pool or a kitty. During the process of collection, any member can draw a lump sum through various ways like a lucky draw, an auction or a member can even fix a payout date based on a known expenditure.

These schemes are very popular in tier II and III towns in India and even in rural India, thanks to under-penetration of banking services, as they are a way of raising quick money or catering for sudden liquidity needs or even a planned expenditure. Also, banks haven't recognised the fact that the common man with a small income finds it very difficult to undergo the entire procedure of getting a loan, adjusting to bank working hours and other demands.

There are many organised companies incorporated to do this as a business and these are governed by state or central laws. There is a central Chit Funds Act of 1982, apart from a number of state chit fund Acts. There is an office of "registrar of chit funds" in every state that monitors operations which are quite stringent. Utilisation and appropriation of subscribers money is strictly prohibited.

The first step of regulation comes at the state level; hence it's the state government which is responsible for any fraudulent activities by chit fund companies.

QIPs

The QIP Scheme is open to investments made by "Qualified Institutional Placement " (which includes public financial institutions, mutual funds, foreign institutional investors, venture capital funds and foreign venture capital funds registered with the SEBI) in any issue of equity shares/ fully convertible debentures/ partly convertible debentures or any securities which are convertible into or exchangeable with equity shares at a later date (Securities).

Since the beginning of 2009, Indian companies are raising billions of dollars from the QIP route.

NBFC

A company is treated as an NBFC if its financial assets are more than 50% of total assets and income from financial assets is more than 50% of the gross income

NBFC means Non-banking financial company. A non-banking financial company (NBFC) is a company registered under the Companies Act, 1956 and is engaged in the business of loans and advances, housing finance, acquisition of shares/stock/bonds/debentures/securities issued by government or local authority or other securities of like marketable nature, leasing, hire-purchase, insurance business, chit business, but does not include any institution whose principal business is that of agriculture activity, industrial activity, ale/purchase/construction of immovable property. NBFCs are similar to banks; however they do not accept demand deposits.

Some microfinance companies are registered as NBFCs and are regulated by the RBI while other MFIs are either registered as money lenders or Societies.
The Reserve Bank of India (RBI) in 2011 approved creation of a separate category of non-banking financial companies for the MFI sector and specified that such institutions need to have a minimum net owned fund of Rs 5 crore.

An RBI-appointed panel headed by Y H Malegam had recommended setting up of a special category of NBFCs operating in the micro finance sector in 2011.These are called Non Banking Financial Company-Micro Finance Institution(NBFC-MFI)..

NBFC factor

The Reserve Bank of India (RBI) in mid-2012 introduced a new category called Non-Banking Financial Company-Factors. Under this new class, a company has to seek registration from the regulator with a minimum net owned fund (capital + reserve) of Rs 5 crore.Thus, Factoring is the business of selling invoices (receivables) to a factoring company (Factor) at a discount . Consequently, the selling corporate can get cash quickly and avoid risk of collecting debt. In India, it is still at a nascent stage. So far, there are around 10 'factors' including SBI Factors and Commercial Services, Canbank Factors, HSBC Factoring and others. Out of all factors, seven or eight companies are on standalone basis. Factoring can be of two types: domestic and export oriented, the latter being called forfaiting. Forfaiting is the purchasing of an exporter's receivables (the amount importers owe the exporter) at a discount by paying cash. The forfaiter, the purchaser of the receivables, becomes the entity to Whom the importer is obliged to pay its debt.

RBI measure will help expand the factoring industry in India.Earlier in January, 2012; the Parliament had passed a bill on the Factoring Regulations Act, 2011 wherein similar proposal were mentioned. The RBI directives came in line with that.

The factoring mechanism mostly assists smaller companies, which run relatively shorter fund flow cycle. Factoring bails them out by supporting their fund system instantly.

ECBs-

ECB (External Commercial Borrowings) is an instrument used to facilitate the access to foreign money by Indian corporations and PSUs (Public Sector Undertakings). ECBs include commercial bank loans, buyers' credit, credit from official export credit agencies and commercial borrowings from the private sector window of Multilateral Financial Institutions such as International Finance Corporation (Washington), ADB and Investment by

Foreign Institutional Investors (FIIs) in dedicated debt funds . ECBs cannot be used for investment in stock market or speculation in real estate. The DEA(Department of Economic Affairs), Ministry of Finance, Government of India along with Reserve Bank of India, monitors and regulates ECB guidelines and policies. In India, External Commercial Borrowings are being permitted by the Government for providing an additional source of funds to Indian corporates and PSUs for financing expansion of existing capacity and as well as for fresh investment, to augment the resources available domestically. ECBs can be used for any purpose (rupee-related expenditure as well as imports) except for investment in stock Market and speculation in real estate.

Applicants are free to raise ECB from any internationally recognised source like banks, export credit agencies, suppliers of equipment, international capital markets etc.

ECB access may be restricted when the there is a deluge of foreign inflows and the rupee is getting strong. It may be relaxed when the opposite happens as we have seen since 2009. ECBs help diversify risk for the companies. Also, the interest rates are softer abroad. They help Indian companies with foreign funds.

Country benefits as it has access to forex.

ECBs can be raised through two routes : Automatic Route and the Approval Route. The former does not require permit from the Regulator whereas the latter requires the same. RBI policy allows corporates registered under the Companies Act, 1956, except financial intermediaries such as banks, financial institutions (FIs), housing finance companies and Non-Banking Finance Companies (NBFCs) to access ECBs. However, in September 2013, 23rd Governor of RBI Raghuram rajan allowed banks to borrow from abroad to meet their Tier 1 requirements of capital(Basel norms will, to be covered later).
NGOs engaged in micro-finance activities have been permitted to raise ECB up to certain limits.

Financial institutions dealing exclusively with infrastructure or export finance such as IDFC, IL&FS, Power Finance Corporation, Power Trading Corporation, IRCON and EXIM Bank are considered on a case-by-case basis.

The priority end use of ECBs includes investment (such as import of capital goods, new projects, modernization/expansion of existing production units) in real sector - industrial sector including small and medium enterprises (SME) and infrastructure sector, power exploration, telecom, railways, roads & bridges, ports and exports.

RBI in June 2012 decided to allow Indian companies to avail of ECBs for repayment, within limits, of Rupee loan(s) availed of from the domestic banking system .Only companies in the manufacturing and infrastructure sector will be eligible to avail of such ECBs.
Policy helps source loans cheap;domesric liquidity constraints are softened;country gets forex;rupee slide could be contained;infrastructure benefits.

Euro issues

Indian companies are permitted to raise foreign currency resources through issue of Foreign Currency Convertible Bonds (FCCBs), ordinary equity shares through Global Depository Receipts (GDRs) to foreign investors i.e. institutional investors or individuals (including NRIs) residing abroad. That is, Euro-issues include Euro-convertible bonds and GDRs.

Private equity

In finance, private equity means equity in companies that is privately placed by the management to a finance firm. It generally has a lock in period during which they are not publicly traded on a stock exchange. Bulk private placement is done.Private equity firm also is given a place in the management of the company . Capital for private equity is raised primarily from institutional investors. The term private equity has different connotations in different countries.

Stock Market (Given as a separate chapter)

Apart from the above mentioned sources of capital for Indian companies from within the country, the International Finance Corporation (IFC) of the World Bank (WB) also provides funds for the private sector. (Given in the chapter on Bretton Woods institutions).

Credit Default Swap

It is a form of insurance against debt default. When an investor buys corporate (or government) bonds he/she faces the risks of default on part of the issuing agent. The investor can insure its investment in such bonds against default through a third party. The investor pays a premium to the party providing insurance. In the event of default by the bond issuer, the insurer would step in and pay the investor. A CDS is just like insurance, which is bought by those who fear default.

Corporate debt

Corporate debt is necessary for their investment, acqusitions etc.

The following are some of the different types of corporate debt securities issued:

Non-Convertible Debentures

Partly- Convertible Debentures

Fully-Convertible Debentures (Convertible into Equity shares)

Bonds

IDF

IDFs are investment vehicles which can be sponsored by commercial banks and NBFCs in India in which domestic/offshore institutional investors, specially insurance and pension funds can invest through units and bonds issued by the IDFs. Infrastructure Debt Funds (IDFs), can be set up either as a Trust or as a Company. A trust based IDF would normally be a Mutual Fund (MF), regulated by SEBI, while a company based IDF would normally be a NBFC regulated by the Reserve Bank.IDF-MFs can be sponsored by banks and NBFCs. Only banks and Infrastructure Finance companies can sponsor IDF-NBFCs. "Sponsorship" means equity participation up to a certain permissible level.

FCCBs (see elsewhere in this chapter)

Bonds are issued to domestic and foreign investors. They are traded on the stock market.

FIIs investment in debt

FIIs can invest in government and corporate debt- primary and secondary market. These limits and the rules are relaxed from time to time depending on the needs of the economy.FII debt is rupee debt.

Take-out financing

It came into effect in 2010. It is a method of providing finance for longer duration projects (for example, 15 years) by banks by sanctioning medium term loans (like 5-7 years). It is the understanding that the loan will be taken out of books of the financing bank within pre-fixed period, by another institution thus preventing any possible asset-liability mismatch.

Under this process, the institutions engaged in long term financing such as IDFC, agree to take out the loan from books of the banks financing such projects after the fixed time period when the project reaches certain previously defined milestones. On the basis of such understanding, the bank concerned agrees to provide a medium term loan, say 5 years. At the end of five years, the bank could sell the loans to the institution and get it off its books. This ensures that the project gets long-term funding though various participants. Banks otherwise cannot lend for infrastructure as their deposits are for a short period and the loans are for a long period- asset liability mismatch.

External sources of financer for India

a. Stock market(partly touched above under Euro issues) like ADRs and GDRs

b. FCCB

c. ECB

d. IBRD and IFC

e. Private equity

f. Bilateral loans by Governments abroad

IFC rupee bond

International investors subscribed to the first ever global rupee bond, setting aside worries about rupee depreciation and other macroeconomic concerns. The first tranche of International Finance Corporation's (IFC) rupee bond saw unprecedented demand from global pension funds, banks, asset management companies and central banks.

The response to the first offshore rupee bond also paves the way for Indian corporates to raise cheaper funds as the currency risk will be borne by the investor.

The bond with a tenor of three years has a coupon of 7.75%, lower than the current G-sec reference rate by 70 basis points.

IFC, which has already raised local currency bonds in Chinese renminbi, Russia's rouble and Brazilian real, proposes to use these funds to finance private sector investment in India.

Internationalisation of rupee(in the class)