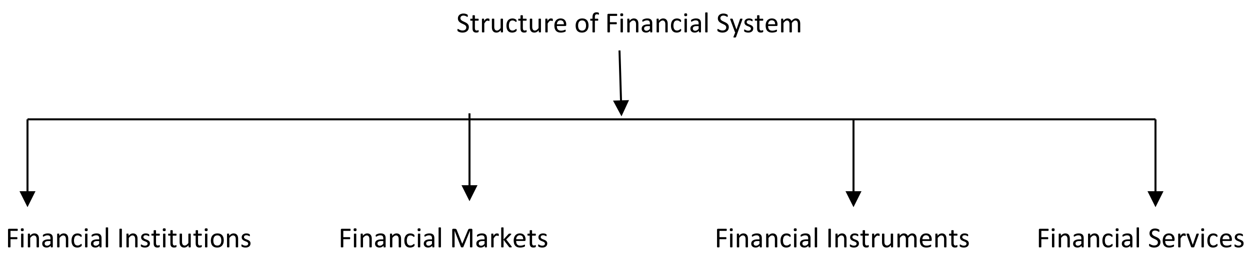
UNIT-I

Financial system may be defined as a set of institutions, instruments & markets which foster savings and channel them to their most efficient use. The Indian financial system consists of the many financial institutions and affects the generation, mobilization & distribution of savings of funds for investment purpose.



These are regulated by Ministry of Finance, Company Law Board (CLB), RBI, IRDA, Department of economic affairs & all these facilities are the process of smooth & efficient transfer of funds.

Financial Institutions:

These are the business organization & they act as a service for the mobilization of savings and provide credit of finance. These also provide various financial services to the public.

Eg: Net Banking, ATM Cards etc……

It can be classified into two types:

a) Banking Financial Institutions:

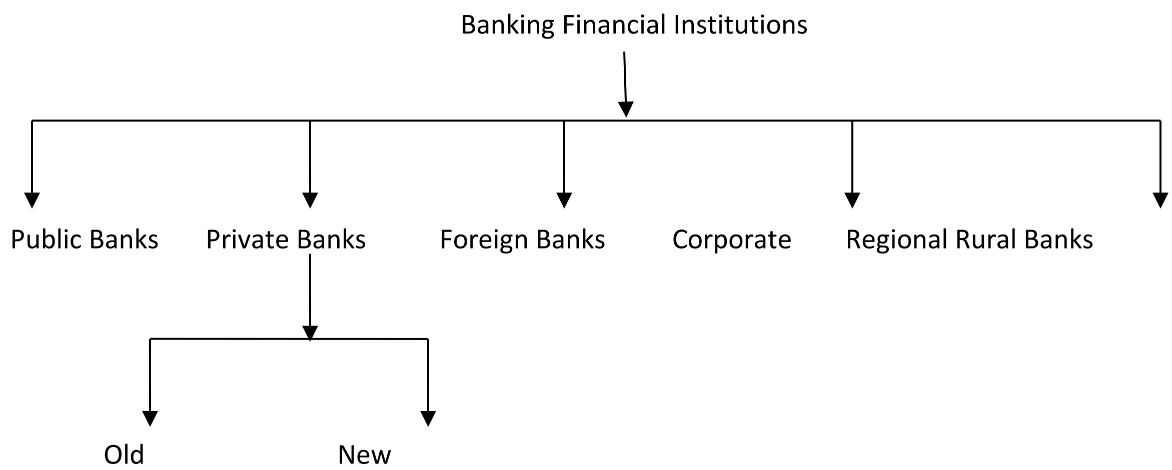
These are those institutions which provide transaction service for the public.

Eg: All Government Banks, Private Banks.

b) Non Banking Financial Institutions:

These are those institutions which provide credit to the public.

Eg: SIDBI,IDBI,NABARD,SFCI’s, IFCI, LIC,GIC etc…….



Banking Financial Institutions	**Non Banking Financial Institutions**
1. The Bank participate in the economies payment mechanism	**1.**The Non Banking Financial Institutions do not participate in the economies payment mechanism
2. These bank provides transaction services like issue of due books, Demand drafts,credit,debit cards	2. These bank don't provides any transaction services
3. Banks creates credit from the savings. Its main function of the banks.	3. It does not create credit.
4.Banks has to fulfill some legal requirements like CRR (Cash Reserve Ratio & SLR (Statuotory Liquid Ratio)	4.They don't have fulfill such legal requirements

Financial Markets:

A Financial market is a place in which financial assets are created or transferred.Financial market are the centers or arrangements that provide facilities for buying & selling of requesting something financial orders & services. The participants in the financial market are corporations, financial institutions, individuals & government.

Classification of Financial Markets:

Financial markets are classified into different ways.

1. On the basis of Financial Claim:

a) **Debt Market:** The debt market is the financial for fixed claim like debt instruments
b) **Equity Market:** It is the financial market for residual claim ie equity instruments

2. On the basis of Marketing:

a) **Money Market:** It is a market where short term funds are borrowed & lend some money. Money market deals in the short term assets a period of maturity of year or less than year which are substitution of money.

   Ex: Treasury Bills, Commercial papers, Certificate of Deposits

b) **Capital Market:** Capital Market is the market for long term funds from the capital market procedure capital raised and made for industrial purpose with maturity period of more than one year.

3. On the basis of Seasoning:

a) **Primary Market:** It deals with issue of new capital. It is also called New Issue Market because that the securities are sold for the first time.

b) **Secondary Market:** A secondary market is a marketplace where already issued securities – both shares and debt – can be bought and sold by the investors. So, it is a market where investors buy securities from other investors, and not from the issuing company.

Financial Instruments:

Financial instruments are those instruments which are used for raising resources for corporate entities. The financial instruments may be classified into :

I. Capital Market Instruments
II. Money Market Instruments

I. Capital Market Instruments:

Capital market is a place where long term funds required by business enterprises provided capital market instruments are equity shares, preference shares, debentures, bond warrants.

Role of a Capital Market Instruments:

Capital Market deals with various types of securities. The securities of the capital market can be classified into:

A. **Industrial Securities or Corporate Securities**
B. **Government Securities or Gilt Edged Securities**

A. Industrial Securities or Corporate Securities:

These are the securities which are issued by Public Companies. Industrial Securities are classified into two types:

a. Ownership Securities
b. Creditor ship Securities

a. Ownership Securities: It mainly includes equity shares & preference shares

i. **Equity Shares:** It may be regarded as the foundation of the financial structure of the company. It contains four values.

- **Face Value** :It is the value of the share stated in the Memorandum of Association & the share certificate.
- **Issue Value**:It is the value issued by the company to a share.
- **Book Value**: It is the value based on the Rate of Reserve & Surplus to the paid up capital
- **Market Value** : Present share value in the market.

Features of Equity Shares:

- Risk Capital
- Fluctuating Dividend
- Fluctuating Market Value
- Voting Right

Rights of Equity Share Holders:

- Right to Income
- Right to Control
- Right to have knowledge of Corporate affairs
- Right to transfer share
- Pre Emptive Right

Classification of Equity Shares in the Market:

- Bluechip Shares
- Growth Shares
- Income Shares
- Defensive Shares
- Speculative Shares

ii. Preference Shares:

These shares represent a particular portion of the share capital which has been endowed with certain preference & unitations.It represents a hybrid security that part taken some characteristics of Equity shares & some characteristics of Debentures.

Types of Preference Shares:

(i) Cumulative preference shares:

A preference share is said to be cumulative when the arrears of dividend are cumulative and such arrears are paid before paying any dividend to equity shareholders.

(ii) Non-cumulative preference shares:

In the case of non-cumulative preference shares, the dividend is only payable out of the net profits of each year. If there are no profits in any year, the arrears of dividend cannot be claimed in the subsequent years.

iii) Participating preference shares:

Participating preference shares are those shares which are entitled in addition to preference dividend at a fixed rate, to participate in the balance of profits with equity shareholders after they get a fixed rate of dividend on their shares. The participating preference shares may also have the right to share in the surplus assets of the company on its winding up.

(iv) Non-participating preference shares:

Non- participating preference shares are entitled only to a fixed rate of dividend and do not share in the surplus profits.

(v) Convertible preference shares:

Convertible preference shares are those shares which can be converted into equity shares within a certain period.

(**vi) Non-Convertible preference shares**:

These are those shares which do not carry the right of conversion into equity shares.

(vii)Redeemable preference shares:

Preference shares which can be redeemed after a fixed period or after giving a certain notice are called a redeemable preference shares.

(viii)Irredeemable preference shares:

Irredeemable preference shares are a perpetual liability, which cannot be redeemed during the lifetime of the company.

Features of Preference Shares:

- Fixed Return
- Return of Capital
- Fixed Dividend
- Non Participating in Property
- Non Participating in Management

B.Creditor ship Securities-Debentures:

Debentures are another kind of security traded in the capital market. A debenture is an acknowledgment of debt by a company.

Features of Debentures:

- A fixed rate of interest is paid in Debentures.
- The maximum Interest paid on payable on these debentures was 14% the recently but how it has been relaxed.
- The interest gained on them is deductible expenditure.
- These are traded on the stock exchange.
- Secured by a charge on immovable property ie we can down on the fixed assets of the company when it is winding up.
- Interest on debentures is payable even there is a loss.

Classification of Debentures:

Debentures may be classified into

1. **On The Basis Of Record Point of View**

a. Registered Debentures

These are the debentures that are registered with the company. The amount of such debentures is payable only to those debenture holders whose name appears in the register of the company.

b. Bearer Debentures

These are the debentures which are not recorded in a register of the company. Such debentures are transferable merely by delivery.

2. **On The Basis Of Security**

a. **Secured or Mortgage Debentures**

These are the debentures that are secured by a charge on the assets of the company. These are also called mortgage debentures. The holders of secured debentures have the right to recover their principal amount with the unpaid amount of interest on such debentures out of the assets mortgaged by the company.

b. Unsecured Debentures

Debentures which do not carry any security with regard to the principal amount or unpaid interest are unsecured debentures. These are also called simple debentures.

3. **On The Basis Of Redemption**

a. Redeemable Debentures

These are the debentures which are issued for a fixed period. The principal amount of such debentures is paid off to the holders on the expiry of such period.

b. Non-redeemable Debentures

These are the debentures which are not redeemed in the life time of the company. Such debentures are paid back only when the company goes to liquidation.

4. **On The Basis Of Convertibility**

a. Convertible Debentures

These are the debentures that can be converted into shares of the company on the expiry of pre-decided period.

b. **Non-convertible Debentures**

The holders of such debentures cannot convert their debentures into the shares of the company.

B. Government Securities or Gilt Edged Securities:

Government securities are called gilt edged securities because the repayment of principal & interest in talks secured by a first charge on the nations purse. These securities are broadly classified into government & securities government securities.

The government securities are classified into classified into central government securities & state government securities guaranted by the central government for all India financial institutions such as IDBI,ICICI & IFCI.

The securities guarantee by state government of state institutions as state electr8icity boards & housing boards & housing boards & treasurer bills issued by bill. The government securities are issued in three forms namely.

1. Stock Certificate or Inscribed Stock:

The stock where the name of the stock holder is inscribed or recorded in the register kept by the public debt office is called inscribed stock.

The stock certificate issued to the holders of the stock shows that has been registered as the owner or a certain amount of government stock.

The title of these stock constant transferred by mere endorsement. A transfer deed will have to be executed for the purpose of transferring it.

2. Promissory Note:

The government's promissory notes are negotiable securities issued by the central or state governments. These rules are certain by the governor for the state government the president for the attested government signed in this note.

3. Bearer Bonds:

Bond whose owner's name is not on record with the bond issuer. Interest accrued on bearer bonds is paid to whoever presents the attached coupons, and the principal is paid to whoever presents the bond for redemption. Ownership (title) of this type of bond can pass from hand to hand by simple delivery, just like a currency note or a bearer

II. MONEY MARKET INSTRUMENTS

1. **Commercial Papers:** These are short term instruments like promisory note with a fixed maturity. They are mostly issued by leading well established & big companies having high credit rating.

Origin:

In India commercial paper has been introduced suggested by the Working Group Committee on Money Market in 1957.

Features:

- Commercial papers can be issued by corpoarate bodies whether financial or Non financial.
- Commercial Papers are normally issued at a discounted and in large denominations.
- The issue of commercial papers should be for a minimum of 25 Lakhs in muktiple of 5 lakhs.
- Prior permission of RBI is required for the issue of Commercial Paper.

2. **Certificate of Deposits:**

Certificate of deposits are short term payable on a fixed date and having short term maturity of not less than 3 months and not more than one year. The issuance of CD's is inmultiple of 5 lakhs subject to a minimum of Rs.25 Lakhs.

Regional Rural Banks & scheduled corporate banks are not supported to issue CD's .Banks are not supported to issue CD's.Banks are not permitted to buy back their CD's before their maturity and the grant loans against their own.CD's can be issued to individuals corporations,companies,trust funds,NRI's.

3. **Treasury Bills:**

Treasury Biils are popularly known as T Bills issued by the government. These bills are highly liquid and these are backed by a guarantee from the government.They are issued for 91 days but now they are also 182 days & 364 days.

4. **Repo:**

The repo are repurchase agreement used by the government security holder.when he/ she sells the security to a lender and promises to repurchase from overnight. Hence Repo's have term ranging from one night to 30 days.

5. **Call Money Market:**

In India the Call Money Market represents the market for Intraback lending & borrowing the loans given in this market for a short term nature.

The maturity of these loans varies between one day & two weeks.They are usually unsecure as these loans are payable within a short period they are considered as a highly liquid & rate of interest is very low & change from day to day.

PRIMARY MARKET OPERATIONS:

The primary capital market deals with issue of the new capital. It is also called New Issue Market because the insecurities are sold for the first time.

The new issue may be classified into two types.

- New companies Issues are also called Intial Issues
- Old companies Issues are also called Further Issues

Purpose:

New securities are issued namely for the purpose of obtaining money or capital funds such issues of securities are called "New Money Issues".

Advantages:

- It provides funds to entrepreneurs for fresh capital investment or for expansion & diversification.]
- But sometimes it may used to pay off debts of the company.In such case they are excluded from the category of new issues. These are:
    - Issue & Bonus shares
    - Exchange Issues

From the operational stand point of view main function of New Issue Market can be classified into three:

a. **Organization:**

It refers to the work of investigating analysis & processing of new proposal. Every new proposal is carefully investigated, analysed & processed by a specialized agency known as Issue House". Issue house carefully studies the technical, economic, financial & legal aspects of the companies which want to raise funds from the primary market.

The services of these issue houses are of advisory in nature. These services include advice as to the time of floatation of an issue and the type the method and the price of an issue.

b. Underwriting:

When shares are issued by a company in the capital market some all of them may not be taken by the public. If the company fails to receive minimum subscription it will have to return the application money.

Every money has to face such uncertainties when they make new issues to help such companies. Some specialized agencies have comeup into the field they are generally called "UNDERWRITERS".

In the case of underwriting the underwriters guarantee that the shares underwriters by thereon will be sold. In case these shares are not taken by the public he will himself purchase the remaining shares and thus the company will be able to obtain subscription for all the shares issue.

Underwriting Agreements are mainly of 3 Types:

a. The underwriting may undertake to purchase the securities which are offered by the issuing company to the public & are not purchased the investor with in a stipulated time.
b. The underwriting may purchase the issue outright for the purpose of resale through their organization.
c. When the issue is very large a single underwriter may not be able to underwrite the whole issue under such circumstances few underwriters will jointly underwrite the issue. This is known as "Syndicate Underwriting".

c. Distribution: The third function of the new issue market is distribution of Shares.Distribution is the function of sales & debentures to the investor.This job is performed by brokers & dealers in securities. They maintain regular and direct contact with the ultimate investors.

LISTING FORMALITIES:

Listing means the admission of the securities of a company for trading on a stock exchange. A Security is said to be listed when its name is included in the list of securities added in a stock exchange. A Company must satisfy the following conditions for listing of securities.

- The minimum issued equity capital of a company should be 3 crores.
- The minimum public offer of equity capital should not be less than 25% of the issued capital.

Objectives:

- Provide ready marketability of stock.
- Ensure liquidity of stocks
- Ensure proper supervision & control of dealings
- Protect the interest of the share holders and the general interest of the public.

Advantages to the Company:

- The listed securities have a greater collateral value for the purpose of raising loan from bankers. The investors prefer to invest their money in such securities. This helps the company raise capital from the market.
- Listing gives greater publicity for the company since the prices of the shares are published in newspapers & magazines.
- Listing not only attracts the general public but also encourage the institutional investors.
- Listing facilitates the general distribution of company securities and thus the company can gain national importance & widespread recognition.

Advantages to the Share Holders or Investors:

- Listing provides liquidity to their holders.
- It helps them to get the best possible prices for their securities when they want to sell.
- The listed securities have a greater promise of share value this will help the holders raise bank finance by these securities.

Basic requirements of listing:

- Memorandum & Articles of Association

- Minimum public offer
- Standard Denominations
- Issue of Prospectus
- Minimum Public Offer
- Allotment of Shares
- Rights issue by a listed Company.

STOCK EXCHANGE

A stock exchange is a marketplace where securities, such as stocks and bonds, are bought and sold. The securities regulation regulation act of 1956 defined stock exchange as “an association, organization or a individual which is established for the purpose of assisting, regulating and controlling business in buying, selling and dealing in securities”

FUNCTIONS OF STOCK EXCHANGES

The stock market occupies an important place in the financial system of our country, which is of vital importance for the proper functioning of the corporate enterprises. At the same time, the stock exchanges are seen as very useful institutions as they provide a variety of services to the investors. Important functions of stock exchanges are briefly explained below.

1. MARKETABILITY OF SECURITIES

Stock exchanges are the markets for purchasing and selling securities. As they provide a ready and continuous market for securities, the securities can be converted into cash without delay.

2. EVALUATION OF SECURITIES

In stock exchanges, prices of securities are determined by investors’ demand and suppliers’ preferences. Stock exchanges integrate the demand and supply of securities and determine their prices on a continuous basis. The prices prevailing in the stock exchanges are called quotations. These quotations enable the investor to evaluate the value of his shareholding.

3. SAFETY OF INVESTMENT

Stock exchanges operate under the rules, bye-laws and regulations duly approved by the government. The members of stock exchange are bound by them. Stock exchanges provide the most perfect type of market by making the transactions publicly known to the investors. Besides this, they avoid over trading and speculation through various regulatory measures. These factors ensure a great measure of safety and fair dealing to the investors.

4. CAPITAL FORMATION

Capital formation occurs due to savings and investments. Stock exchanges facilitate capital formation in the country. They create the healthy habit of saving, investing and risk bearing among the investors. The prices quoted in stock exchanges indicate the extent of popularity of companies. Investors are attracted towards profitable companies and come forward to invest their savings in the corporate securities. Thus, stock exchanges facilitate flow of capital into more profitable channels.

5. REGULATION AND MOTIVATION OF COMPANIES

Companies wishing to list their shares on a stock exchange should follow certain rules and regulations. For example, every year, they should submit to stock exchange all relevant data relating to their financial affairs. So, the listing companies will safegurad their interest by monitoring their financial performance carefully. Thus, the stock exchanges by quoting the prices of securities motivate the companies concerned to improve their financial performance.

6. FACILITATES FOR HEALTHY SPECULATION

Speculation is taking advantage of fluctuations of price movement. With regard to securities market, healthy speculation is essential to equate demand and supply of securities at different places. Further, it regulates the prices of securities to a great extent. The mechanism of stock exchanges encourages healthy speculation thereby enabling the shrewd investors to benefit from price fluctuations.

7. BAROMETER OF BUSINESS PROGRESS

Stock exchanges reflect the prevailing business conditions in the country. Booms and depressions are reflected by the index prices of various securities traded in the stock exchange. By analyzing the causes for such changes in business conditions, the government can take suitable fiscal measures.

REGULATION OF CAPITAL MARKET:

The Government has taken a no of administrative actions and made loss for the growth and working of the financial system in India. .The y following are the important acts passed by the parliament.

1) The capital issue control act 1947
2) The India companies act 1956
3) The securities contract Regulation act 1956
4) The monopolies & Restrictive trade practices (MRTP) act 1970
5) The foreign exchange regulation act 1973
6) The securities is exchange Board of India act (SEBI) 1992

THE CAPITAL ISSUE CONTROL ACT 1947:

CCI working on the concept of exercising a control on the capital market activities with special emphasis the primary market activities.

It used to exercise strict control through the following system on the companies entering the primary market.

1) Pricing of the issue
2) Timing of the issue
3) Capital structure of the company.
4) Permission for the issue.

THE INDIAN COMPANIES ACT 1956:

According this act gave guidelines regarding.

1) Issue of share capital

2) Issue of New shares
3) Further issue of shares
4) Issue of shares at premium
5) Issue of shares at discount
6) Provision relating to allotment of shares

SECURITIES CONTRACT REGULATION ACT 1956:

The principal objectives of passing this act are.

1) Give wide range powers to the central government to control security transactions and regulate stock market price.
2) Creation of well organized and efficient securities market.
3) Reform and improve the working of stock exchange.
4) Check the exercise and undesirable speculative activities.
5) Ensure protection to investors
6) Minimize academic development through.
7) Assist academic development through channeling savings into investments.

MRTP ACT MONOPOLES &RESTRICTIVE PRACTIES ACT 1980:

The objectives of MRTP act are

1) To control monopolies & to Regulate Monopolies with trade practices.
2) To regulate unfair trade practices.

FOREIGN EXCHANGE REGULATION ACT (FERA) 1970

FERA was passed in 1973 to regulate foreign investment in India Industries .The important provision of this act are;

1) Any investments in India by foreign National foreign company have to be made only with the approval of RBI.
2) Proposal for issue of shares including Bonus non-resident share holders and transfer of shares by non-resident share holders to Indian Resident need the approval of RBI.

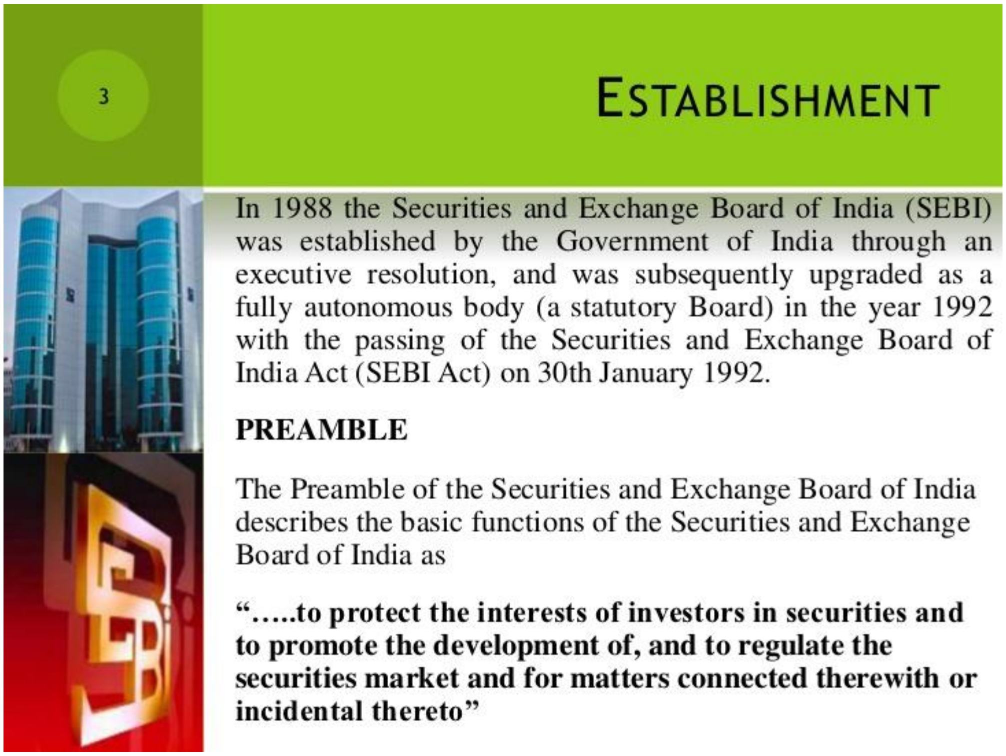
3) Remittance of dividends on equity to non-resident share holders is permitted in certain cases without the approval of RBI.

SEBI ACT 1992

The act was implement t in May 1992 and it replaces CCI act .It aims to regulate the following.

1) Primary Market Activities
2) Secondary Market Activities
3) Intermediaries of capital market
4) Companies
5) Investor
6) Structural change in capital market

ROLE OF SEBI:



Reasons for Establishment of SEBI:

With the growth in the dealings of stock markets, lot of malpractices also started in stock markets such as price rigging, 'unofficial premium on new issue, and delay in delivery of shares, violation of rules and regulations of stock exchange and listing requirements. Due to these malpractices the customers started losing confidence and faith in the stock exchange. So government of India decided to set up an agency or regulatory body known as Securities Exchange Board of India (SEBI).

The Organisational Structure of SEBI:

1. SEBI is working as a corporate sector.

2. Its activities are divided into five departments. Each department is headed by an executive director.

3. The head office of SEBI is in Mumbai and it has branch office in Kolkata, Chennai and Delhi.

4. SEBI has formed two advisory committees to deal with primary and secondary markets.

5. These committees consist of market players, investors associations and eminent persons.

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FUNCTIONS OF SEBI

The SEBI Act, 1992 has entrusted with two functions, they are

- Regulatory functions And
- Developmental functions

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REGULATORY FUNCTIONS

- Regulation of stock exchange and self regulatory organizations.
- Registration and regulation of stock brokers, sub-brokers, Registrars to all issues, merchant bankers, underwriters, portfolio managers etc.
- Registration and regulation of the working of collective investment schemes including mutual funds.
- Prohibition of fraudulent and unfair trade practices relating to securities market.
- Prohibition of insider trading
- Regulating substantial acquisition of shares and takeover of companies.

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Developmental Functions

- Promoting investor's education
- Training of intermediaries
- Conducting research and publishing information useful to all market participants.
- Promotion of fair practices
- Promotion of self regulatory organizations

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Powers of SEBI

- Power to call periodical returns from recognized stock exchanges.
- Power to compel listing of securities by public companies.
- Power to levy fees or other charges for carrying out the purposes of regulation.
- Power to call information or explanation from recognized stock exchanges or their members.
- Power to grant approval to bye-laws of recognized stock exchanges.

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POWERS OF SEBI CONTINUE..

- Power to control and regulate stock exchanges.
- Power to direct enquiries to be made in relation to affairs of stock exchanges or their members.
- Power to make or amend bye-laws of recognized stock exchanges.
- Power to grant registration to market intermediaries.
- Power to declare applicability of Section 17 of the Securities Contract (Regulation) Act 1956, in any State or area, to grant licenses to dealers in securities.

Role of the Financial System in Economic Development

Economic development is partially dependent on the financial system to help mediate the transfer of money to areas of the economy that need it most. The financial system has a number of key functions, which help facilitate these shifts in money that are important for sustainable economic growth.

The following are the roles of financial system in the economic development of a country

- Savings-investment relationship
- Financial systems help in growth of capital market
- Government Securities market
- Financial system helps in Infrastructure and Growth
- Financial system helps in development of Trade
- Employment Growth is boosted by financial system
- Venture Capital
- Financial system ensures Balanced growth
- Financial system helps in fiscal discipline and control of economy
- Financial system's role in Balanced regional development
- Role of financial system in attracting foreign capital
- Financial system's role in Economic Integration
- Role of financial system in Political stability
- Financial system helps in Uniform interest rates
- Financial system role in Electronic development

FINANCIAL SERVICES SECTOR PROBLEMS

- Lack of Expertise
- Inadequate Accommodation
- Inadequate Technology
- Inadequate Quality Service
- Captive Organization

- Restricted scope of operations
- Limited Innovation
- Lack of sound Institutional Mechanism
- Other Problems

FINANCIAL SECTOR REFORMS

Financial sector reforms are centre point of the economic liberalization that was introduced in India in mid-1991.

The elements of the financial sector are Banks, Financial Institutions, Instruments and markets which mobilize the resources from the surplus sector and channelize the same to the different needy sectors in the economy. The process of accumulative capital growth through institutionalization of savings and investment fosters economic growth

ORIGIN

The economic reform process occurred amidst two serious crisis involving the financial sector the balance of payments crisis that endangered the international credibility of the country and pushed it to the edge of default; and the grave threat of insolvency confronting the banking system which had for years concealed its problems with the help of faulty accounting strategies.

Some deep rooted problems of the Indian economy in the early nineties were also strongly related to the financial sector such as large scale pre-emption of resources from the banking system by the government to finance its fiscal deficit.

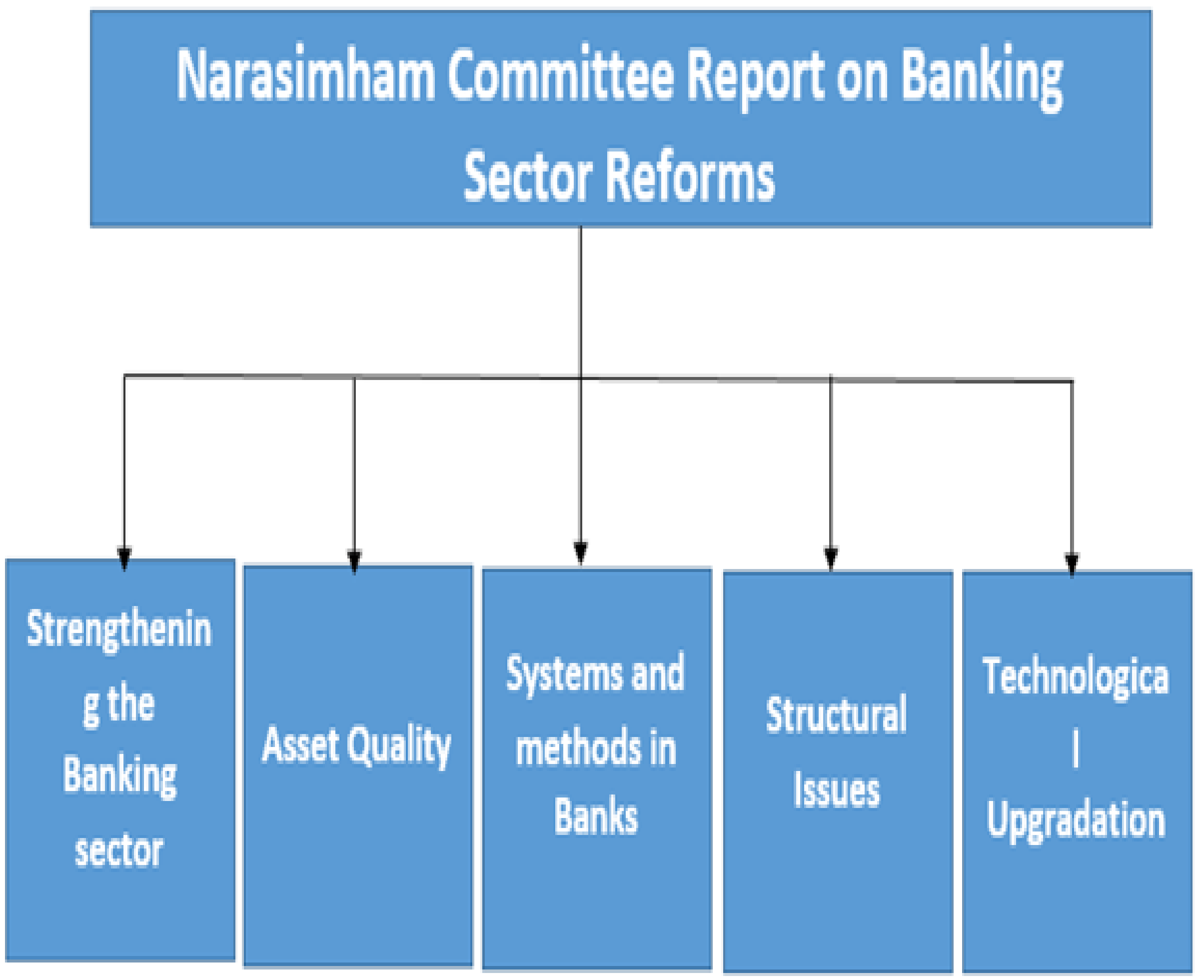
Financial and banking sector reforms are in following areas:

- Financial markets
- Regulators
- The banking system
- Non-banking finance companies
- The capital market
- Mutual funds
- Overall approach to reforms

- Deregulation of banking system
- Capital market developments
- Consolidation imperative

Regulators

- The Reserve Bank of India (RBI)
- Securities and Exchange Board of India (SEBI) and
- Insurance Regulatory and Development Authority (IRDA)

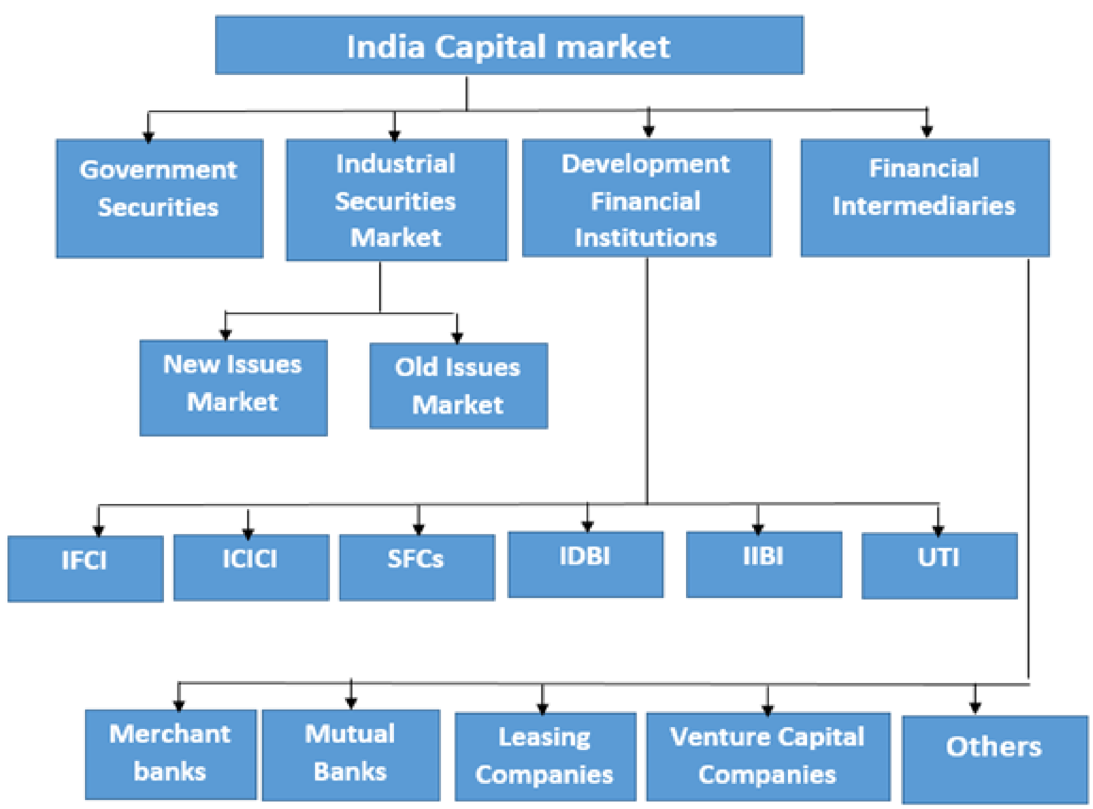


Forex market reform:

Forex market reform took place in 1993 and the successive adoption of current account convertibility were the acmes of the forex reforms introduced in the Indian market. Under these reforms, authorised dealers of foreign exchange as well as banks have been given greater sovereignty to perform in activities and numerous operations. Additionally, the entry of new companies have been allowed in the market. The capital account has become effectively adaptable for non-residents but still has some reservations for residents.

Capital Market Reform

Capital market is defined as a financial market that works as a channel for demand and supply of debt and equity capital. It channels the money provided by savers and depository institutions (banks, credit unions, insurance companies, etc.) to borrowers and investees through a variety of financial instruments (bonds, notes, shares) called securities.



The Regulatory Framework

- SEBI has implemented a modern regulatory framework with rules and regulations to control the behaviour of major market participants such as stock exchanges, brokers, merchant bankers, and mutual funds.
- It has also sought to control activities such as takeovers and insider trading which have implications for investor protection.
- The governing structure of stock exchanges has been changed to make the boards, of the exchanges more broad based and less dominated by brokers.
- SEBI acts as a supervisor of the system undertaking supervision of the activities of various participants including stock exchanges and mutual funds and violations of the rules are punishable by SEBI.

Opening the Capital Market to Foreign Investors

Significant policy initiative in 1993 was the opening of the capital market to foreign institutional investors (FIIs) and allowing Indian companies to raise capital abroad by issue of equity in the form of global depository receipts (GDRs).

Modernization of Trading and Settlement Systems

Major developments occurred in trading methods which were highly antiquated earlier. The National Stock Exchange (NSE) was established in 1994 as an automated electronic exchange. It empowered brokers in 220 cities all over the country to link up with the NSE computers and trade in a unified exchange with automatic matching of buy and sell orders with price time priority, thus ensuring maximum transparency for investors. The initiation of electronic trading by the NSE generated competitive pressure which forced the BSE to also introduce electronic trading in 1995.

Futures Trading

Currently, an important gap in India's capital market is future markets. Good market in index futures would help in risk management and provide greater liquidity to the market.

Mutual Funds

Presently, the mutual funds industry is controlled under the SEBI (Mutual Funds) Regulations, 1996 and amendments thereto. With the issuance of SEBI rules, the industry had a framework for the setting up of many more companies, both Indian and foreign firms. The Unit Trust of India is biggest mutual fund controlling a quantity of nearly Rs.70,000 crores, but its share is going down. With the growth in the securities markets and tax advantages granted for investment in mutual fund units, mutual funds became widespread. The foreign owned AMCs are the ones which are now setting the pace for the industry. They are introducing new products, setting new standards of customer service, improving disclosure standards and experimenting with new types of distribution.

Reform of the Insurance Sector

The Insurance sector in India directed by Insurance Act, 1938, the Life Insurance Corporation Act, 1956 and General Insurance Business (Nationalisation) Act, 1972, Insurance Regulatory and Development Authority (IRDA) Act, 1999 and other related Acts. The basis of liberalizing the banking system and encouraging competition among the three major participants' viz. public sector banks, Indian private sector banks, and foreign banks, applies equally to insurance. There is a strong case for ending the public sector monopoly in insurance and opening it up to private sector participants subject to suitable prudential regulation.

Conclusion

To summarize, the financial sector is main element of the Indian economic system.

Financial experts suggested that there is a need for effective reforms to ensure that this remains competitive and attractive for investors from across the world. The economic reforms have preferred the need for changing the policy objective to promotion of industries and the formation of more integrated infrastructural facilities.

UNIT - II

Financial service sector:

Service that is financial in nature is known as financial services and these are part of financial system.

Financial service refers to the service provided by the financial industry .The finance industry for encompasses a broad range of organization that deal with management money.

These companies are Banks, mutual funds, insurance companies etc;

NATURE OF FINANCIAL SERVICES:

1) Financial services are intangible in nature.
2) Financial services are inseparable from the provider.
3) Financial services are customer centric.
4) Financial services are dynamic in nature.

TYPES OF FINANCIAL SERVICES:

1) Merchant Banking
2) Leasing
3) Hire-purchase
4) Venture capital
5) Mutual Funds
6) Factoring
7) Forfeiting
8) Insurance
9) Credit Rating
10) Credit Cards
11) Depository Service
12) G Brokerage Service

SCOPE OF FINANCIAL SERVICE:

Financial service cover a wide range of activities .They can be broadly classified into two categories' and these are.

1) Traditional Activities

2) Modern Activities

1) **TRADITIONAL ACTIVITIES:**

Traditionally the financial intermediaries have been rendering a wide range of service encompassing both capital and money market activities these are again divided into two types.

A) Fund Based Activities

B) Non-Fund Based Activities

A) **FUND BASED ACTIVITIES:**

The fund based financial services are also called Asset Based financial service and they include the following services.

1) Lease Financing
2) Hire purchase Finance
3) Factoring and Forfeiting
4) Housing Finance
5) Insurance services
6) Venture capital Financing

B) **Non-Fund Based Activities:**

1) Managing the capital issue i.e.; Mgt. of pre –issue and post-issue activities.

2) Arrangement of funds from financial institution for project cost or working capital requirements.

3) Assisting in the process of getting all govt.and other clearness.

2) **MODERN ACTIVITIES:**

Most of these Modern activities are non –fund based activities.

1) Rendering project advisory services right from the preparation of the funds project report till the raising of funds first starting of the report with necessary Govt. approval.
2) Planning for Mergers & acquisition and assisting for their smooth carry out.
3) Guiding corporate customers in corporate restructuring.
4) Managing the portfolio of large Public Sector Corporation.
5) Undertaking services relating to capital market such has
   a) Clearing services
   b) Registration and transfer of securities.
   c) Collection of income and securities
6) Promoting credit rating agencies for the purpose of rating companies which want to go public by the issue of debt instrument.

REGULATION OF FINANCIAL SERVICES IN DIA:

The Indian financial service sector is regulated by.

1) Government
2) The RBI
3) The SEBI

1) **GOVERMENT:**

The central Govt has power to regulate the financial services sector with in exercise control by various acts, rules, directives. guidelines, notification etc;

The issue of capital is regulated by the companies' act 1956 and the capital issue (control) 1947.

The stock exchanges are regulated by the securities contract regulation act 1956 and the securities contracts regulation rules 1957.

2) **THE RESERVE BANK OF INDIA:**

The Reserve Bank of India has wide power to control the money is capital markets. It ensures the efficient functioning of the financial system by keeping a watch on developments.

It influences the operations of the financial system through regulation on the Banking system.

3) **THE SECURITIES EXCHANGE BOARD OF INDIA:**

The SEBI was established in the year 1992 and it.

- ❖ Protect the interest of the investors in securities.
- ❖ Promote the development of the securities market.
- ❖ Regulated the securities Market.

SEBI is authorized to regulate all merchant Banks on issue activities and to regulate mutual funds by issuing guidelines and supervising.

MERCHANT BANKING:

Merchant Banking is a basket of financial services provided by the merchant banker .The merchant Banker is an organization registered with SEBI as a merchant Banker and providing all or any of the following services.

1) Issue mgt
2) Underwriting
3) Broker to the Issue
4) Project mgt.
5) Project Consultancy
6) Loan Syndication
7) Portfolio Mgt
8) Portfolio Consultancy

DEFINITION OF MERCHANT BANKING:

According to SEBI (Merchant Bankers) rules 1992 , Merchant Banker is "Any person who is engaged in the Business of issue management either by making arrangement regarding ,selling, buying or subscribing to securities as a manager consultant or rendering corporate advisory services in relation to such issue management".

TYPES OF MERCHANT BANKING:

The merchant banks could be classified into the following 3 categories.

1) Division of commercial Banks.
2) National & state level Financial Corporation such has ICICI, IFCI&SFC'S.
3) Leading Broker Firms.

ROLE OF MERCHANT BANKERS:

The following services are provided by merchant Bankers.

I) ISSUE MANAGEMENT:

The capital issue mgt concerned with the mgt of issue for raising capital through various types of instruments by corporate enterprises .It is a professional service rendered by Merchant Bankers.

The steps involved in the issue management are:

1) Pre issue mgt.
2) Post issue mgt up to listing of securities on the stock exchange.

1. PRE ISSUE MGT:

It involves the following function in respect of issues through prospectors.

1) Obtaining Approval for the issue from SEBI.
2) Drafting prospectors and getting it approved by various Agencies concerned.
3) Arranging Underwriting for the purposed issue.
4) Drafting and finalization of other forms documents such has application forms newspaper advertisements and other stationary requirements
5) Selection of register to the issue, printing, press, Advertising Agencies, Brokers & to the issue.
6) Arranging press conferences for Brokers and investors.
7) Deciding the opening &closing dates of the issue.
8) Determining about the Branches from where Application money should be collected.

2. POST ISSUE MGT:

It includes the following activities.

1) Getting the daily Report of application money collected at various Branches.
2) Obtaining subscription to the issue (It is nothing but underwriting)
   Note: All underwriters are merchant Banker but not vice versa.
3) After the close of issue getting consent of the stock exchange for deciding the basis allotment .
4) Sending compliance Report to the SEBI.
5) Obtaining letter from the regional stock exchange approving the basis of allotment for different categories.
6) Sending copy of the letter of the regional stock exchange to other stock exchange where the company wants to list.
7) Confirm the listing formalities have been complied with.
8) Obtaining permission for allotment of shares and debentures to NRI'S&FII'S
   NRI: Non Resident Indians.
   FII: Foreign Institutional Investors

II) UNDERWRITING:

Under writing is a process, which gives guarantee to the minimum subscription of the companies public issue .Moreover SEBI has made underwriting compulsory for the company for the public subscription.

III) CORPORATE COUNSELLING:

The merchant Banker offers the following services to the corporation.

1) Economic Analysis of product Ranges, cost, analysis, pricing strategies etc;
2) Financial Analysis including mgt of working capital, Long Term cost of capital and project mgt.
3) Legal Counseling.

IV) GOVT CONSENT/ PERMISSION:

These services include.

1. Obtaining necessary approvals licenses and permission from the government for industrial projects.
2. Guiding promoters in the matter of rules and regulations of government.

V) CREDIT SYNDICATION OR LOAN SYNDICATION:

It involves raising of finance with the help of consortium of Banks and financial institution .The merchant Banker render syndication services to their clients and thus they help their clients to raise rupee and foreign loans for long term.

They negotiate with the participating Banks and financial institution.

VI) PORTFOLIO MANAGEMENT:

The merchant bankers take up mgt of portfolio of securities on behalf of their clients. These services include.

1) Advertising on investment in Govt securities.
2) Under taking purchase and sale of securities.

3) Management of Individual Investment portfolio Management service.

VII) NON –RESIDENT INVESTMENT:

In order to attract NRI Investment in primary &secondary market the merchant Banker provide the following investment advisory services to (NRI'S)

1) Identification of Investment opportunities.
2) Selection Management
3) Portfolio Management.
4) Purchase &sale of securities.
5) Securing the necessary clearance from RBI & FERA for payment of interest &dividends.

VIII) ADVISORY SERVICES RELATED TO MERGER & TAKE OVER:

In this regard the merchant Banker renders the following services.

1) Appraisal of the merger or takeover proposals with respect to financial viability technical feasibility.
2) Negotiation with the concerned parties.
3) Determination of the appropriate exchange Ratio.
4) Assistants relating to procedural &legal aspects.
5) Obtaining necessary Approvals.

REGULATION OF MERCHANT BANKING:

The merchant Banking Activities are regulated by.

1) Guidelines of SEBI & the Ministry of Finance.
2) Companies Act 1956
3) Listing Guidelines of Stock Exchange.
4) Securities Contract Regulation Act 1956

CONCLUSION:

The merchant Banking activity these covering especially issue and underwriting of shares and debentures are regulated by the SEBI (merchant Banker regulation 1992.

SEBI may inspect the books account records and documents of merchant Bankers.

1) To ensure that the books of accounts are maintained in the required manner.
2) To verify that the provision of the acts, rules and regulation are complied with.
3) To investigate complaints against merchant bankers.

LEASING:

The European leasing association defines as "A contract between a Lessor & a Lessee for hire of a specific asset selected by the lessee".

Note: Lessor — Owner of the Asset.

Lessee __ User of the Asset

The Lessee can have possession and use of the asset on payment of Specific Rentals over a period.

In simple terms Leasing refers to a contract which the owner of an asset allows another person to use the asset in returns of some rent.

FEATURES OR LEASING:

1) It is a contract as defined in the Indian contract act 1872.
2) Leasing is an agreement between the owners of the equipment called "lessor" and the user called "lessee".
3) The goods are delivered to the "lesser" for a specific purpose &period.
4) The lessee should return exactly the same goods after the lease period.
5) The owner ship of the goods is retained by their less or and only the possession of the goods is given to the lesser.
6) The good are delivered to the lessee in return for a periodical rent.

TYPES OF LEASES

Following types of leases are provided

1) Financial Lease
2) Operating Lease
3) Sale & lease Back
4) Cross border lease
5) Dry vs. wet
6) Big ticket
7) Leveraged

1. FINANCIAL LEASE:

A Lease agreement which satisfies any of the following two conditions is called as financial lease.

1) Lease term or lease period should be equal or more than 75% of the life of the asset.
2) Present value of the lease rental is equal to or more than 90% of the value of the asset.

FEATURES OF FINANCIAL LEASE:

1) These are non cancellable
2) These are dry –maintains &insurance is the responsibility of lessee.
3) Lessor does not provide for the upgradation or exchange replacement of the asset.
4) Generally these are for immovable properties like land, house etc;

2. OPERATING LEASE:

An operating lease is a lease agreement for a short time period. This type of lease is undertaken for office equipment computers &machinery.

FEATURES OF OPERATING LEASE:

1) These have a provision for cancellation for either party after giving a notice as per agreement.
2) Lessor provides for the upgradation and maintenance of the asset.
3) These leases can be dry or wet.
4) Tenure of lease is shortened as compared to the life of the asset.

3. **SALE & LEASE BACK:**

It is a lease agreement in which the previous owner of the asset becomes “Lessee” and the purchaser becomes the “Lessor” .This type of lease agreement involves the following steps.

1) Owner of the asset sells the asset to another party with the condition to take it back on lease.
2) The previous owner becomes the “Lessee” and the new purchaser becomes the “Lessor”.
3) “Lessee” pays the lease rental according to the terms of agreement.
4) At the end of the lease term asset reverts back to the “Lessor”.

4. **CROSS BORDER LEASE:**

These leases are again divided into types those are.

1. Import lease
2. International lease

i. IMPORT LEASE:

It is a lease transaction in which both the Lessor &Lessee are domiciled in the same country where as the asset supplier is domiciled in a different country and the asset is imported for the purpose of lease.

ii. INTERNATIONAL LEASE:

It is a type of lease agreement in which Lessor & Lessee both are domiciled in different countries. This lease agreement is governed according to the respective rules and regulations of both the countries involved.

The main purpose of such lease transaction is to have depreciation tax benefit for both the parties resulting from the difference in the tax laws.

5. **DRY VS WET LEASE:**

A Dry lease transaction is such a transaction in which the Lessor does not provide in which the maintenance and insurance of the asset instead all such expanses are borne by the lessee is termed as the dry lease.

A Wet lease transaction is such a transaction is such a transaction in which the Lessor provides for the maintain and insurance of the asset.

6. BIG TICKET LEASE:

When the value of the asset being leased out is very high is termed as big ticket lease. Like lease of an aircraft, ship, Dam or other heavy items or infrastructure.

7. **LEVERAGED LEASE:**

It is a type of lease agreement in which the less or arranges for a special loan to finance the asset to be leased out.

UNIT -III

VENTURE CAPITAL:

International finance corporation Washington (IFCW) defines venture capital as equity or equity featured capital seeking investment in new ideas ,new companies ,new products, new processes or New services that offer a n potential of high returns on investment.

FEATURES OF VENTURE CAPITAL:

1) Investments are generally made in equity
2) Investments are made in new enterprises using new technology y to produce new product in expectation of higher gains.
3) The venture capital investor maintains a close contract with the enterprepreneur to safeguard his investment but does not interfere with the mgt of then enterprises.
4) Venture capitalist approach differs from the stock market investor and the banker he continuously keeps a close watch over Business.
5) Venture capital investment is not liquid .The venture capitalist cannot realize his money on demand .There is no repayments' schedule.
6) The investment is lost if the enterprise is unsuccessful.

VENTURE CAPITAL FINANCE

Early Stage Financing

*Speed capital

*Startup capital

*Second- round finance

Later Stage Financing

*Expansion Finance

*Replacement/Development Finance

*Management Buy-Out

* Management Buy-Ins

*Turn around

Financing pattern of Venture Capital or Steps for Venture Capital Finance:

Stages of Finance:

It is divided into two types: I. Early Stage Finance II.Last Stage/Later Stage Finance

I. **Early Stage Finance:** This stage includes:

a. Seed Capital: It refers to the capital requires by a entrepreneur for conducting research at pre-commercialization stage. It is provide by the venture capitalistic for translating an Idea into a business proposition.

b. **Startup capital:** It refers to the setting up of the firm or a company. At the stage firm or a company is ready to manufacture of a product or service provider. This start up of finance is providing the capital institutions.

c. **Second Round Financing:** This financing is required at the stage at which the product as already being launched in the market. At this stage the business is not in a position to earn the profits.

II. **Early Stage Finance:** This stage of venture capital involves establishes business which required additional financial support. It involves the following types of capital.

a. **Expansion Finance:**

The venture capital institutions provide the finance for the purpose of expanding business like adoption of technology, plant location in different countries or different areas etc….

b. **Development Finance:**

The Venture capital provide a finance to develop the business such as making of different product lines, providing different types of services to their customer's establishment of plant.

c. **Management Buy –Outs :**

A management team buying out a company that they already work it is known as Management Buy Out (MBO)

In other words it's a form of admission where a company existing manager acquires a large part of all the company from the either parent company or subsidiary**.**

d. **Management Buy- Ins:**

It refers to the buying of another business is known as Management Buy- Ins (MBI).In other words a corporate action in which an outside management is purchase an ownership & replacement of existing management Is known as MBI.This type of action occurred due to having poor management team.

e. **Turn Around:**

The financial required of a company has been performing poorly for an extend time. In order to an efficient a turnaround a company must knowledge & identify the problems, consider changes in management & develop a problem solving strategy. The problems of companies are:

- Revenue does not Cover the cost
- Inability to pay the amount for the creditors
- Declining the stock price & inability to pay the salary for their employees

Legal Aspects & Guidelines of Venture Capital:

1. Guidelines of Established of Venture Capital Companies (VCC):

1) Funds companies or schemes wishing to undertake venture capital financial activities may be established using the term venture capital and they should agree to abide by these guidelines.
2) Approval should be given for the establishment of VCC/VCF by the department of economic affairs ministry of finance.

3) All India public sector financial institutions ,SBI other scheduled banks including foreign banks operating in India and the subsidiaries of the above could be eligible to start VCC/VCFA, subject to such approval as may be required from the reserve bank of India in respect of Banking companies joint ventures b/w t venture capital companies could be permitted.

2. Guidelines for Management of VCC/VCF:

1) It is required that the Venture Capital Funds or Venture Capital Companies (VCF or VCC) are managed by professionals such has bankers managers & administrators &persons with adequate experience in industry, finance accounts.
2) No persons would be permitted to be the full-time chairman, president, chief executive, managing director or executive director or a old time director of a venture capital company or venture capital fund .If he holds any of the above position in another company.

3. Guidelines for Venture Capital Assistance:

Venture Capital Assistance is provided for the enterprises which fulfill the following perimeters.

1) SIZE: The total investment not to exceed 10crore.

2) TECHNOLOGY: New or relatively untried or which incorporate some significant improvement over the existing areas in India

3) PROMOTERS (OR.) ENTERPRENEURS:

Relatively new, professional or technically qualified with adequate resources or being to finance the project.

Investment in enterprise engaged in trading Broking .financial services shall not be permitted.

4. Guidelines Regarding VCC/VCF:

The minimum raise funds from the size of VCC/VCF would be 10crore.It desires to raise funds from the public the promoters share shall not be less than 40%.

5. Guidelines Regarding DEBT -EQUITY RATIO:

Debt equity ratio may be maximum of 1:1.5.

6. Guidelines Regarding UNDERWRITTING &LISTING:

The VCC/VCF may be listed according to the prescribed norms. It issue may be underwritten at the discretion of the promoters.

GROWTH OF VENTURE CAPITAL IN INDIA:

In India the venture capital industry has been sponsored by financial institutions &Banks like **IDBI, ICICI,UTI,IFCI, SBI&CANARA BANK ETC;**

Some of the country's leading venture capital companies are:

1) IDBI 'S VCF
2) Technology Development & Information Company of India ltd. (TDICI)
3) ANZ Grind lays Bank (India Investment Fund)
4) Credit Capital Venture Fund India Ltd corporation ltd.
5) Risk Capital & Technology Finance Corporation Ltd (RCTC).
6) 20^{th} century Venture Capital Corporation Ltd.
7) Andhra Pradesh Industrial Development Corporation (APIDIC) Venture Capital Ltd.
8) Canara Bank Venture Capital Fund.
9) Gujarat Venture Finance Ltd. (GVFL)
10) SIDBI Venture Capital Fund
11) SBI Venture Capital Fund
12) Infrastructure Leasing & Financial Services (IL &FS) Venture Corporation
    (Infrastructure leasing &financial service)

FACTORING:

Factoring is a debt collection service where the factor –usually a financial institution –Buys out clients (seller) book debts (accounts receivable)

Factoring means purchase of Book debts of clients (companies). Factoring is financial service designed to help firm in better management of their receivables and this is called “Para –Banking” practice in the developed countries.

MEANING OF FACTORING:

Factoring is a type of financial service where by a firm sells or transfer title to its accounts receivable to a factoring company. Which then acts as principal, not as agent .The receivables are sold without resource meaning that the factor cannot turn to the seller in the event of accounts prove to be uncollectable.

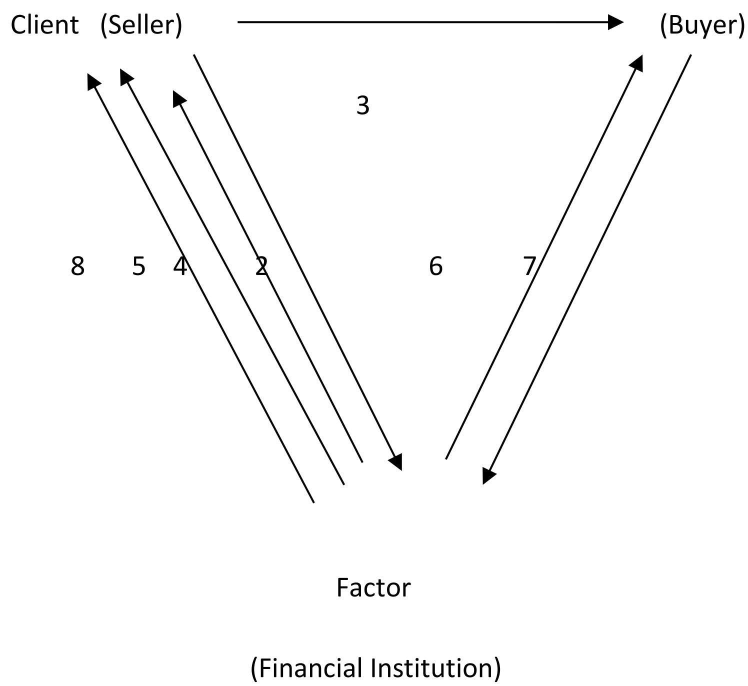
DEFINITION

Factoring is also defined as a relationship between the financial institution or banker and a business concern (the supplier), selling goods or providing service to trade customers (the customers where by the factor purchase book debts either with or without resource to the supplier and in the relationship thereto control credit extended to the customers and administers the sales ledger of the supplier.

STEPS INVOLVED IN FACTORING:

1) The customer places an order with the seller.
2) The factor and the seller enter into a factoring agreement about the various terms of factoring.
3) Sale contract is entered into with the buyer and the goods are delivered. The invoices with the notice to pay the factor are sent along with.
4) The copy of invoice covering the above sale is said to the factor who maintains the sale ledger.
5) The factor prepays 80% of the invoice value.
6) Monthly statements are send by the factor to the buyer .If these are any unpaid invoices follow up action is initiated.
7) The Buyer settles the invoices on expiry of credits period allowed.
8) The Balance 20% less the cost of factoring is paid by the factors to the client

$$\text{Company} \xleftarrow{\quad 1 \quad} \text{Customer}$$



TYPES OF FACTORING ARRANGEMENT:

1) Recourse & Non –Recourse Factoring
2) Advance &Maturity Factoring
3) Domestic &International Factoring
4) Undisclosed Disclosed Factoring
5) Limited &Full Factoring

RECOURSE &NON- RECOURSE FACTORING:

Under the resource factoring arrangement the factor has the right to demand payement from the supplier (or) client. In the event of default by the customers.

This means the factor does not bear credit risk associative with receivables.

In this case the factor charges the client for maintaining the sales ledger and debt collection services.

Under the Non –Recourse factoring the factor bears the risk bad debits for this a high commission change is collected by factor from the company**.**

ADVANCE &MATURITY FACTORING:

Under the advances factors a factor provides advance against factor receivable at an agreed interest rate. The amount to be advance is pre –farcified and ranges from 75 to 90%. The balance is paid after the collection is over.

Under the maturity factoring , when the factor does not made a pre-payment to the client it is known as maturity factoring .This factor the following administrative service.

1) Monitoring and Maintain sales ledger.
2) Issuing and dispatching Invoices
3) Collecting debts on sale due date.

DOMESTIC AND INTERNATIONAL:

In the domestic forecasting factoring all the exporter three parties (client , customer, factor) involved buyer (customer) seller (client)&factor are domiciled in the same country.

In the International Factoring there are four patties involved and they are Exporter, Importer, Export Factor,& Import Factor (customer, client).southern ,India are it was jointly promoted by canard bank ,Andhra bank ,SIDBI,.The first private sector factoring company foremost factoring ltd command its operations from 1997.

FULLFACTORING & LIMITED FACTORING:

Full factoring is the most comprehensive from of factoring. It combines the features of almost all the factoring services. I t is also known as old-line factoring. It provides the entire spectrum of service, namely, collection, credit, sales ledger administration, and short-term finance.

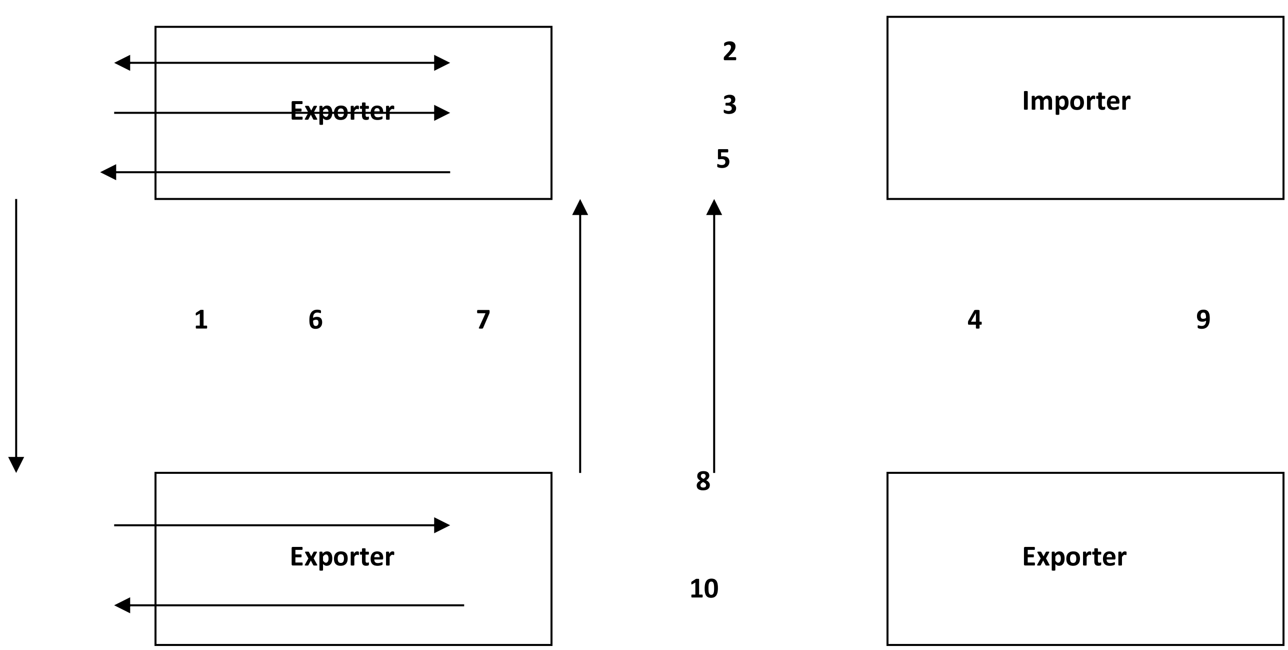
Whereas limited factoring factor only provides limited services.

FORFEITING:

Forfeiting is a financial tool to exporters enabling them to control their credit sales into cash sales by discounting their receivables with an agency called forfitor.It is not only a financial tool but also an important risk management. Tool to exporters be by selling the export receivables to the forfeiters the exporter is relieved of the risk involved in International Trade.

Steps involve forfeiting process:

1. Forfeiter commits to purchase deal from the exporter.
2. Commercial contract between exporter and importer
3. Delivery of goods from exporter to importer
4. Bank gives guarantee
5. Importer hand over documents to exporter
6. Exporter delivery document to the forfeiter
7. Forfeiter pays cash without recourse to the exporter.
8. Forfeiter present the documents to bank of maturity payment
9. Importer repurchase bank & maturity
10. Bank replaces forfeiter at maturity.



Some of the forfeiting services provide in International Trade. There are

- Standard Bank London
- Hongkong Bank
- ABN Amro Bank
- EXIM Bank
- IFC Bank
- Indo Avale Bank

Difference b/w factoring &forfeiting:

FACTORING	FORFEITING
1. Factoring provide only Short term finance.	1.Forefaiting provides medium term finance the credit period ranges b/w 1to 5 yrs
2.It provides both domestic and export Business.	2. It provides finance only for export Business.
3. Factoring involves the purchase of the book debts clients	3. Forfeiting involves the purchase of the export bill (Or) receivable.
4. Financing involves financing administration of the ledger Assumption of credit risk,Recovery of debtors& redressing ,Consultancy services.	4. It is pure financing arranged.
5. The factoring arrangement may be recourseable or non recourseable.	5.Forfeiting arrangement is non-recourseable arrangement

BILL DISCOUNTING:

While discounting a bill the Bank Buys the bill before its before its due and credits the value of the bill after a discount charge to the customer's account.

In other wards bill discounting is a process of converting a bill into cash a\t less than its past value before its maturity

UNIT -IV

CREDIT RATING

INTRODUCTION:

According to Credit Rating Agencies Regulation 1999 rating means. An Opinion regarding securities expressed in the form of standard symbols assigned by a credit rating agency like CRISIL, ICRA, and CARE used by an issuer of such securities

"A credit rating estimates the credit worthiness of an individual, corporation (or) even a country". A credit rating is also known as an evaluation of a potential borrower's ability to repay debt.

A poor credit rating indicates a high risk of defaulting on a loan and thus leads to high interest rates or the refusal of the loan by the creditors.

CREDIT RATING AGENCIES IN INDIA:

CRISIL: Credit Rating Information Service of India Limited

CRISIL is the first credit rating establish in India. It was promoted jointly by ICICI,UTI in 1987.There are a number of other shareholders such as ADB,LIC,HDFC,GIC.It commence its operation on 1ST Jan 1988 in Mumbai. It provides the following services to corporate.

- Rating Services
- Information Services
- Advice Services

IICRA: Investment Information and Credit Rating Agencies of India Limited

It has promoted by the IFCI & there are by the share holders namely SBI,LIC,GIC,EXIM Bank, Bank of India is start with operation in 1991.It is the second most important credit rating agency in India after CRISIL.It provides the following services.

- Rating of Credit Instrument
- Equity Rating
- Credit Assessment

CARE: Credit Analysis and Research

It is promoted by the IDBI jointly with investment institutions, banks and other finance companies. It commences its operations October 1993.The instruments credit rated by CARE are Debentures, Fixed Deposits, Certificate of Deposits, Commercial Papers.

Duff &Phelps Credit Rating India Pvt Ltd (DPCRI)

It is the latest credit rating business in thecountry.it is joint venture between the International Credit Agency Duffs & Phelps & M.J.Financial and Allianz Group. It provides the following rating services.

- Debt Instruments
- Companies & Countries on their request
- Commercial papers

In August 1996 the RBI accused agency commercial paper in India.

ONICRA: Onida Individual Credit Rating Agencies in India.

It is the first rating agency establish in India to rate the credit worthiness of Non –Corporate or Individual business. It was sponsor by Onida Finance Limited.

It does not rate the individual but analysis the risk associated with entering transaction with a particular individual particular point of time. Hence this kind of credit rating useful for the issue of Credit Cards, granting of housing loans, leasing or hire purchase, personal loans ,bank finance etc….

DEBT RATING SYSTEM OF CRISIL&ICRA&CARE:

CRISIL	ICRA	CARE	SIGNIFICANCE
AAA	LAAA	CAREAAA	Highest Safety
AA	LAA	CAREAA	High Safety
A	LA	CAREA	Adequate safety
BBB	LBBB	CAREBBB	Moderate safety
BB	LBB	CAREBB	Inadequate safety
B	LB	CAREB	Risk prone
C	LC	CAREC	Substantial Risk
D	LD	CARED	Default

Note: Rating symbols for long term debt instruments. Long term debt instruments include debentures Bonds is preference shares

RATING SYMBOLS FOR MEDIUM TERM DEBT INSTRUMENTS:

CRISIL	ICRA	CARE	SIGNIFICANCE
FAAA	MAAA	CAREAAA	Highest Safety
FAA	MAA	CAREAA	High Safety
FA	MA	CAREA	Adequate safety
FB	MB	CAREBBB	Inadequate safety
-	-	CAREBB	Inadequate safety
-	-	CAREB	Inadequate safety
FC	MC	CAREC	Risk prone
FD	MD	CARED	Default

Note: Medium term Debt instruments refer to fixed Deposits.

RATING SYMBOLS FOR SHORT TERM DEBT INSTRUMENTS:

CRISIL	ICRA	CARE	SIGNIFICANCE
P1	A1	PR1	Highest Safety
P2	A2	PR2	High Safety
P3	A3	PR3	Adequate safety
P4	A4	PR4	Risk prone
P5	A5	PR5	Default

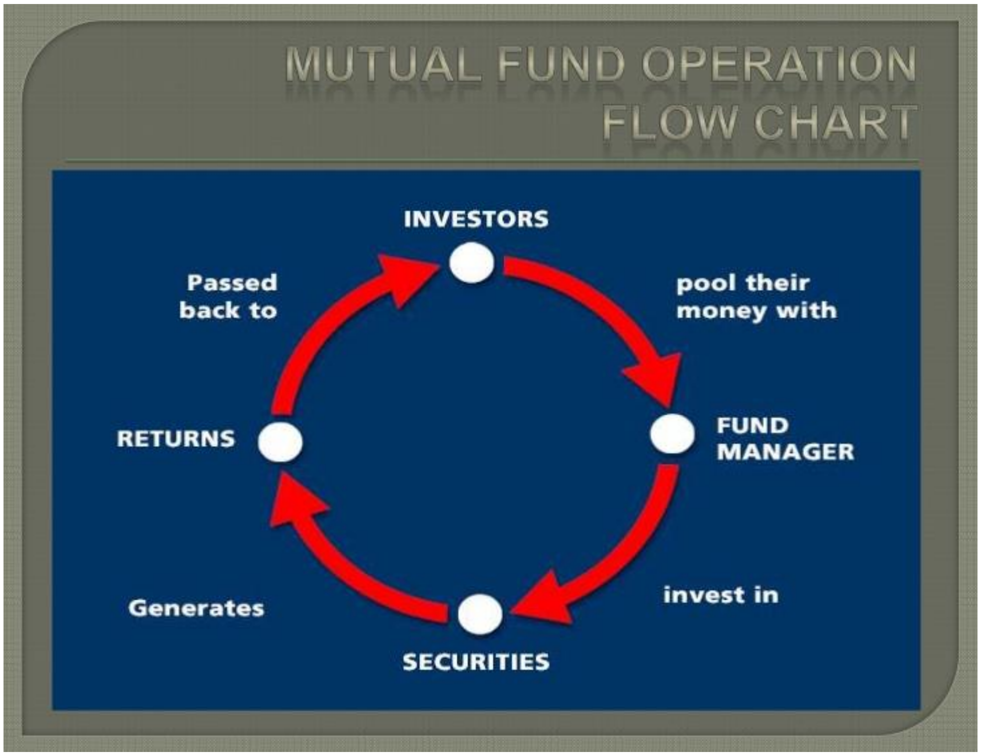
Note: short term Debt Instrument includes commercial papers only.

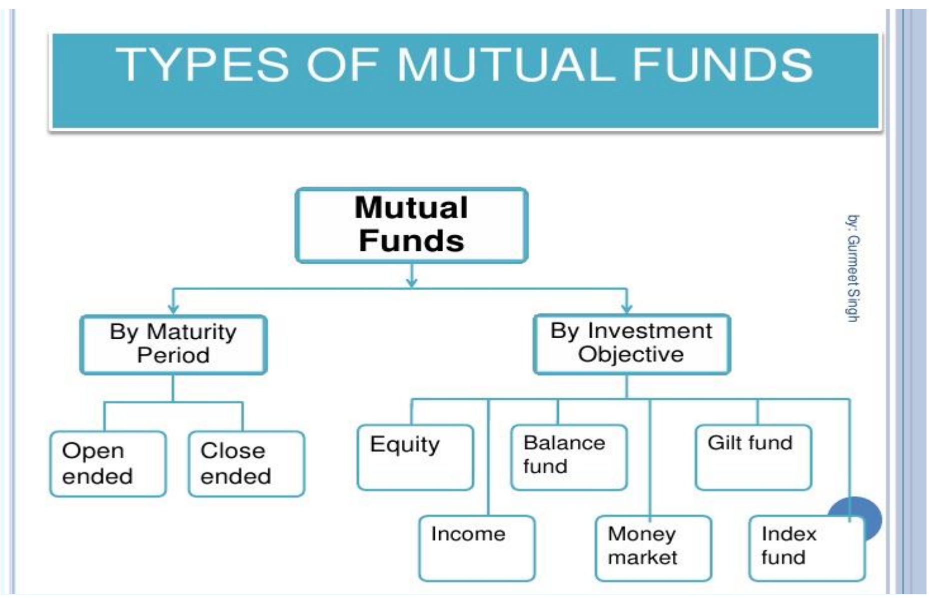
MUTUAL FUNDS

A Mutual Fund is a trust that pools the savings of a number of investors who share a common financial goal. The money thus collected is then invested in capital market instruments such as shares, debentures and other securities. The income earned through these investments and the capital appreciation realized is shared by its unit holders in proportion to the number of units owned by them.

Thus a Mutual Fund is the most suitable investment for the common man as it offers an opportunity to invest in a diversified, professionally managed basket of securities at a relatively low cost.

Investors of mutual funds are known as unit holders.


MUTUAL FUND OPERATION
FLOW CHART
INVESTORS
pool their
money with
FUND
MANAGER
invest in
SECURITIES
Generates
RETURNS
Passed
back to


TYPES OF MUTUAL FUNDS
Mutual
Funds
By Maturity
Period
By Investment
Objective
Open
ended
Close
ended
Equity
Balance
fund
Gilt fund
Income
Money
market
Index
fund
by: Gurmeet Singh

Schemes according to Maturity Period

A mutual fund scheme can be classified into open-ended scheme or close-ended scheme depending on its maturity period.

Open-ended Fund

An open-ended Mutual fund is one that is available for subscription and repurchase on a continuous basis. These Funds do not have a fixed maturity period.

close-ended Fund

A close-ended Mutual fund has a stipulated maturity period e.g. 5-7 years. The fund is open for subscription only during a specified period at the time of launch of the scheme.

by: Gurmeet Singh

Fund according to Investment Objective

A scheme can also be classified as growth fund, income fund, or balanced fund considering its investment objective.

Growth / Equity Oriented Scheme

The aim of growth funds is to provide capital appreciation over the medium to long- term.

Such funds have comparatively high risks.

These schemes provide different options to the investors like dividend option, capital appreciation, etc.

by: Gurmeet Singh

Income / Debt Oriented Scheme

The aim of income funds is to provide regular and steady income to investors.

Such schemes generally invest in fixed income securities such as bonds, corporate debentures, Government securities and money market instruments.

Such funds are less risky compared to equity schemes

by: Gurmeet Singh

Balanced Fund

The aim of balanced funds is to provide both growth and regular income as such schemes invest both in equities and fixed income securities in the proportion indicated in their offer documents.

These are appropriate for investors looking for moderate growth.

by: Gurmeet Singh

Money Market

These funds are also income funds and their aim is to provide easy liquidity, preservation of capital and moderate income.

These schemes invest exclusively in safer short-term instruments such as treasury bills, commercial paper and government securities, etc.

These funds are appropriate for corporate and individual investors as a means to park their surplus funds for short periods.

by: Gurmeet Singh

Gilt Funds

These funds invest exclusively in government securities.
Government securities have no default risk.

Index Funds

This schemes invest in the securities in the same weightage comprising of an index.

This schemes would rise or fall in accordance with the rise or fall in the index

by: Gurmeet Singh

Advantages

Mutual funds have advantages compared to direct investing in individual securities. These include:

- Increased diversification
- Daily liquidity
- Professional investment management
- Ability to participate in investments that may be available only to larger investors
- Service and convenience
- Government oversight
- Ease of comparison

Disadvantages

Mutual funds have disadvantages as well, which include:

- Fees
- Less control over timing of recognition of gains
- Less predictable income
- No opportunity to customize

ORGANIZATION STRUCTURE OF MUTUAL FUNDS

Mutual Fund Shareholders:

The Mutual Fund Shareholders, like the other share holders have the right to vote. The voting rights include, the right to elect directors during the directorial elections, voting right to approve the alterations investment advisory contract pertaining to the fund and provide approval for changing investment objectives or policies.

Board of directors:

The Board of directors supervise the functional activities, which include approval of the contract Asset Management Company and other various service providers.

Investment Management Company or Asset Management Company:

This body handles the mutual fund portfolio as per the objectives and policies mentioned in the prospectus of the mutual funds.

Custodians:

The custodians protect the portfolio securities. Mostly qualified bank custodians are used for mutual funds.

Transfer Agents:

The transfer agent for the purpose of maintaining records and similar functions. The maintenance of the shareholder's accounts, calculation of dividends to the be disbursed, sending information to the shareholders about the account statements, notices, and income tax information. Some of the transfer agent sends information to the share holders about the shareholder transactions and account balances. They also maintain customer service departments in order the cater to the queries of the shareholders.

SEBI:

The primary aim of the Securities Exchange Board of India is to protect the interest of the mutual fund investors. The SEBI has formulated several policies for better functioning and controls the mutual funds. In the year 1993, SEBI issued guidelines pertaining to the mutual funds. All mutual funds, private sector and public sector are regulated by the guidelines of the SEBI. The Asset Management Company managing the funds has to be approved by the SEBI.

Mutual Fund Objectives

Here are some of the main forms of mutual fund objectives that we commonly see:

- **Growth Mutual Funds** – Probably the most common mutual fund objective is investing for growth. . A growth mutual fund simply wants his assets to appreciate over time. Growth mutual funds are generally invested primarily in the stock market and include stock market sectors from small to large cap.
- **Income Mutual Funds** – The second more common mutual fund objective is investing for income. Many investors – typically those who are older and looking for cash flow to supplement their income – want an income distribution from their investment. Income mutual funds typically

will distribute cash payments based on how many shares you own every month and the income generally varies over time. Most income mutual funds will invest in all types of bonds as well as some high quality dividend paying stocks and hybrids like preferred stocks.

- **Socially Responsible Mutual Funds** – Some investors prefer to invest with social responsibility as their focus. There are various types of socially responsible mutual funds.
- **Sector Mutual Funds** – Some mutual funds will invest only in a specific sector, such as biotechnology or healthcare. This provides them exposure to advances in smaller sections of the economy, such as when money floods into technology sectors due to the advent of a faster computer chip or more stable programming platform.

GUIDELINESS FOR MUTUAL FUNDS:

1) Mutual funds are to be established in the form of a trust under the Indian Trusts Act,1882 and operated by separate asset management companies.(AMC)
2) They have to set up a board of Trustees companies and constitute their Board of Directors.
3) The AMC's and trustees are to be two separate legal entities and an arm length relationship must be maintained between the two.
4) The AMC'S are required to furnish SEBI their respective Memorandum and Articles of Association for approval.
5) Mutual Funds dealing exclusively with money market instruments (such has CD'S, Cps and bill discounting) are to be regulated by the Reserve Bank of India.
6) All schemes floated by Mutual funds are to be registered with SEBI.

WORKING OF PUBLIC & PRIVATE MUTUAL FUNDS:

PRIVATE COMPANY:

1) ABN AMRO Mutual fund 15 April 2004
2) Birla sun life mutual fund 1999
3) HDFC Mutual fund 30 June 2000
4) Reliance Mutual fund 1995
5) Standard chartered mutual fund 2000
6) Franklin Templeton India mutual fund

PUBLIC COMPANY:

1) UTI 1964
2) SBI Mutual Fund 1987
3) Cañar Bank Mutual Fund
4) Indus Bank Mutual Fund
5) Bank of India Mutual fund
6) Punjab National Bank Mutual fund

Debt Securitization

Debt secularization is loan which is given from financial institution to borrowers. But these debts of loan are given in the form of security or marketable instrument. Suppose, A gives loan to B. Loan is an Fixed asset for A and it is fixed liability of B. Now, B gives loan to C. But this loan is given in the form of marketable instrument. Now, it is current asset of B.

1st Party: Originator

This is the main organization. It gives loan in the form of loan not in the form of debt securitization. In this party, we can include RBI or SBI.

2nd Party: Special Purpose Vehicle

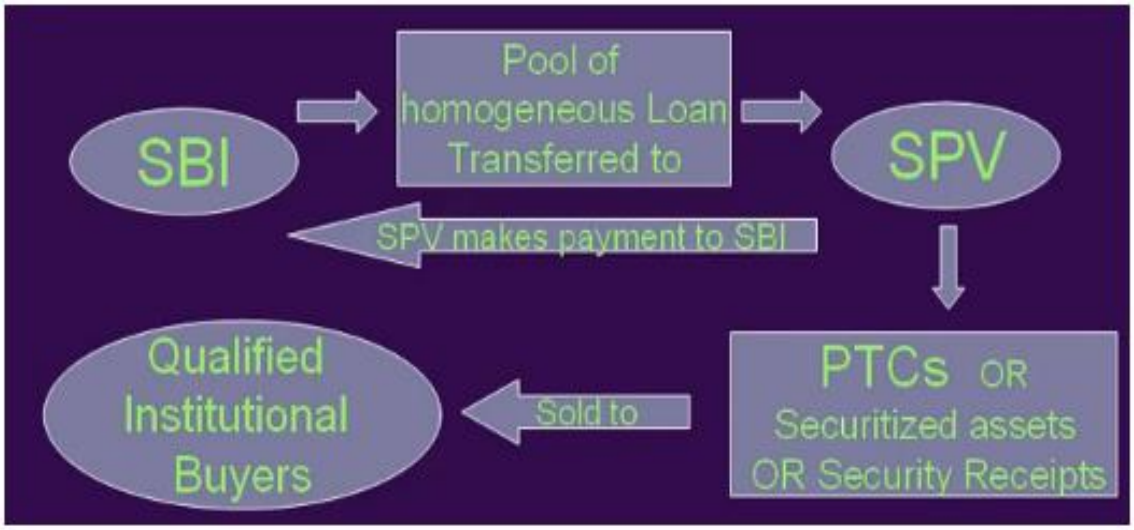
Special Purpose vehicle are that party who gets loan or pool of loan from originator and convert it in marketable securities. After converting it in marketable securities or papers or Demat, it will become debt securitized. Now, SPV will sell it in the money or any other financial market. These parties include private banks and other private financial institution which you can find their office in your local city.

3rd Party: Qualified Institutional Buyers

Now SPV advertises for his debt securitization product. But they did not sell to all. SPV sells to those who clear its condition. All these parties are called QIN.

Example:

Suppose, SBI finds 10 SPV and gave loan of Rs. 200 Crores. Now, 10 SPV converts this Rs. 200 loan in the form of debt securitization and sells to different qualified buyers. These buyers may be 1000 or 100000. One of the best benefits of debt securitization is to reduce risk. If SBI gives Rs. 200 crores to one party. It may be risky. But to give 10 SPV is less risky. For SPV, market instruments are also less risky to give 100000 persons. Following is its Graph.



DEMAT (DEPOSITORY) SERVICES

Financial services relating to holding maintaining g and dealing in securities in electronic form by a financial intermediary known as depositary participant are called ('**DEMAT or depository services)**There are four parties in a demat transaction;. The consumer, the Depository participant (DP), the depository, and the share Register and transfer Agent (R&T) .In India, a demat account, the abbreviation for dematerialized account, is a type of banking account which dematerializes paper-based physical stock shares. The dematerialized account is used to avoid holding physical shares: the shares are bought and sold through a stock broker.

Origin:

This account is popular in India. The Securities and Exchange Board of India (SEBI) mandates a demat account for share trading above 500 shares. As of April 2006, it became mandatory that any person holding a demat account should possess a Permanent Account Number (PAN), and the deadline for submission of PAN details to the depository lapsed on January 2007.

Purpose:

When you buy company shares, you receive share certificates. You need to preserve them safely and need to produce them for any transaction, which is time taking. Instead, if you opt for DEMAT (De-Materialization), you can convert them electronically as balance in your account. (Just like your bank account - you can deposit, keep, withdraw or transfer). A DMAT account is an account which is electronically maintained by the Banks or is provided by Broker agencies where you can keep money for transactions in Shares, Mutual Funds, purchase of Gold etc. It has to be tagged with your Savings account from where the money will be paid if you purchase a share etc and receive money when you sell a share etc

Procedure:

1.Fill demats request form (DRF) (obtained from a depository participant or DP with whom your depository account is opened).

2. Deface the share certificate(s) you want to dematerialize by writing across Surrendered for dematerialization.

3. Submit the DRF & share certificate(s) to DP. DP would forward them to the issuer / their R&T Agent.

4. After dematerialization, your depository account with your DP would be credited with the dematerialized securities.

The benefits

-A safe and convenient way to hold securities;

- Immediate transfer of securities;

- No stamp duty on transfer of securities;

- Elimination of risks associated with physical certificates such as bad delivery, fake securities, delays, thefts etc.;

- Reduction in paperwork involved in transfer of securities;

- Reduction in transaction cost;

Required Documents

- A canceled check, preferably MICR
- Proof of Identification
- Proof of Address
- Proof of Pan card (mandatory)
- Recent photographs, one and, or more

The steps of depository process are as follows:

Step-1: opening an account

Step-2: Dematerialization

Step-3 : Rematerialization

Step 4: Distributing Dividend

Step 5 : Closing an Account

STEP 1: OPENING AN ACCOUNT:

An investor who wants to avail of the services will have to open an account with the depository through a DP, who could either be a custodian a bank ,a broker or individual with a minimum net worth of 1`crore.

STEP2: DEMATERIALIZATION:

To convert his physical holdings of securities into the dematerialized form the investor makes an application to the DP in a Dematerialization Request form (DRF) within seven days the DP forwards the form along with the security certificates to the issuer or its registrar and transfer agent electronically registering the request with the depositary.

STEP3: REMATERIALIZATION:

To with draw his security balance with the depository the investor makes an application to the depository through its (DP). He request for the withdraw of balance in his account in a Remeterialization. Request form (RRF) On receipt of the RRF , the participant checks whether sufficient free revel ant security balance is available in the client account .If there is the participant accepts the RRF and blocks the balance of the client to the extent of the rematerialization quantity and electronically forward the request to the depository.

STEP4: DISTRIBUTING DIVIDENT:

A company (issuer) or its registrar and transfer agent shall make known the depository of the corporate actions such has dates for book closures redemption or maturity of security conversion of warrants and call money from time-to –tine.

STEP5: CLOSING AN ACCOUNT:

A client wanting to close an account shall make an application in the format specified to that effect to the participant. The client may close his account if no balances are outstanding to his credit in the accounts.

NSDL (National Securities Depositary Limited)

NSDL, the first and largest depository in India, established in August 1996 .This depository promoted by Industrial Development Bank of India, Unit Trust of India, National Stock Exchange of India Limited, and State Bank of India was registered on June7, 1996 with SEBI and commenced operations in November 1996.

For the economic development of the country .has since established a national infrastructure of international standard that handles most of the trading and settlement in dematerialized form in Indian capital market.

AIM:

- To Use innovative and flexible technology systems.
- To support the investors and brokers in the capital market of the country.
- To ensure the safety and soundness of Indian marketplaces by developing settlement solutions that increase efficiency,
- Minimize risk and reduce costs.
- To develop financial services industry.

Role of NSDL:

NSDL interacts with investors and clearing members through market intermediaries called depository participants. NSDL performs a wide range of securities related functions through the DPs. These services are as follows:

(1) Maintenance of individual investors' beneficial holdings in an electronic form.
(2) Dematerialization and re-materialization of securities
(3) Account transfer for settlement of trades in electronic shares.
(4) Allotments in the electronic form in case of initial public offerings
(5) Distribution of non-cash corporate actions.
(6) Facility for freezing/locking of investor accounts.
(7) Facility for pledge and hypothecation of securities.

CDSL(Central Depository Services (India) Limited:

CDSL is the second depository set up by the Bombay Stock Exchange (BSE) and co-sponsored by the State Bank of India, Bank of India, Bank of Baroda, and HDFC bank,.

AIM:

The main aim is to provide convenient, dependable services at affordable prices to all the market participants. According to SEBI norms any one can act as depository participant (DP) which includes banks, financial institutes, or even a stock broker and many more.

Person who wants to invest in this field is popularly known by the name beneficial owner has to open a DMAT account through any of the depository participant for holding and transferring securities. A person who wants to open a CDSL need to fill a CDSL modification form. CSDL modification form is mandatory to be filled by every depository participant. CSDL modification form is not complicated to be filled because it is easy to fill the CSDL modification form online and at the same time it can be submitted online.

ORIGIN:

Central depository services India limited received a certificate for business by SEBI in February 1999.

- CSDL started the operating in July 15 1999 when union finance minister flagged the operation.
- National stock exchange, Delhi stock exchange, Calcutta stock exchange and many other lading stock exchanges in India got connected with central depository services India limited.

Functions of CDSL and NSDL which are:

- Main investors holding in an electronic form which is the main function performed by CDSL and NSDL.
- Another function of CDSL and NSDL is surrender and withdrawal of securities to and from the depository.
- Settlements of traders which are done by stock exchange of India are done by CDSL and NSDL.

UNIT -V

MICRO FINANCE

Microfinance refers to an array of financial services, including loans, savings and insurance, available to poor entrepreneurs and small business owners who have no collateral and wouldn't otherwise qualify for a standard bank loan.

Microfinance is a way to promote economic development, employment and growth through the support of micro-entrepreneurs and small businesses; for others it is a way for poor to manage their finances more effectively and take advantage of economic opportunities while managing the risks.

The terms have evolved - from micro-credit to micro-finance, and now it is known as 'financial inclusion'.

Goal

The goal of microfinancing is to provide individuals with money to invest in themselves or their business to help get them out of poverty. When providing loans, microfinancing institutions do not require collateral, but do insist that the loan is repaid within six months to a year.

History of microfinance

While the concept has been used globally for centuries, it's Bangladesh's Muhammad Yunus who is credited with being the pioneer of the modern version of microfinance. While working at Chittagong University in the 1970s, Yunus began offering small loans to destitute basket weavers. Yunus carried on this mission for nearly a decade before forming the Grameen Bank in 1983 as a way to reach a much wider audience.

Today, the Grameen Bank's 2,500 branches serve more than 8 million borrowers in roughly 81,000 villages. According to Grameen Bank, its clients, 97 percent of whom are women, repay loans more than 97 percent of the time, a recovery rate higher than any other banking system. In 2006, Yunus and Grameen Bank were jointly awarded the Nobel Peace Prize for their microfinancing work.

Who are microfinance clients?

Microfinance is aimed at poor people with low income having no opportunity to use services of formal financial agents, for instance, banks. They are often self-employed microentrepreneurs operating small businesses. In urban settings, these can be market stall, grocery shop, car repair or other workshops while in rural localities, such business is usually focused on agriculture, food processing, livestock, and poultry raising. More than a half of microfinance clients all over the world are women.

Key features of microfinance

prefers women customers over men	provides tiny loans for short terms	prefers saving over borrowing
does not take security	offers cost which covers interest rates	provides financial services to the poor and very poor

Products common used in the microfinance sector today is:

- **Micro savings** –In SHGs the members save small amounts of money, as little as a few rupees a month in a group fund.. As SHGs prove capable of managing their funds well, they may borrow from a local bank to invest in small business or farm activities. Banks typically lend up to four rupees for every rupee in the group fund;
- **Micro insurance** –s. The is different types of insurance services like life insurance, property insurance, health insurance and disability insurance.
- **Micro leasing** – For entrepreneurs or small businesses who can´t afford buy at full cost they can instead lease equipment, agricultural machinery or vehicles. Often no limitations of minimum cost of the leased object;
- **Money transfer** – A service for transferring money, mainly overseas to family or friends. Money transfers without opening current accounts are performed by a number of commercial banks through international money transfer systems such as Western Union , Money Gram, and Anelik
- **Remittances** and **microfinance**, and **defined** it as “a condition in which **microfinance** institutions offer. **remittance** transfers in underserved areas through an effective market presence, selling tailored financial.
- **Micro Credit -** Microcredit is a part of microfinance. As a rule, microcredit is targeted at unsalaried borrowers having no or little collateral. This term does not typically include consumer credit extended to salaried employees and built upon automated credit scoring system. In turn, microfinance presents financial services and products, such as money transfers, savings, insurance, and other services offered by different providers.

- **MICRO-PENSION-**

Ujjivan and IIMPS launch Micro-Pension scheme for women

Ujjivan,one of India's leading microfinance institutions in partnership with IIMPS (Invest India Micro-Pension Services) launched two micro-pension products for over 10 lakh urban poor women across India. On 8th April, over 300 microfinance customers attended a pension awareness function in Pune. The program also marked the launch of the scheme.

"We cannot build better lives with 1 or 2 year thought process. Development happens when we integrate today with tomorrow and Micro-Pensions is a step towards Financial Inclusion rather than just a financial product", said Jolly Zachariah. He shared the progress Ujjivan has made in micro credit serving over 10 lakh customers nationally.

This partnership model with IIMPS will deliver an integrated and well regulated financial solution to financially-excluded households at an affordable cost. The model harnesses the network of Ujjivan's 301 branches in 20 states (including 48 under-banked districts) around the country, enabling women in low income households to accumulate micro-savings for their various lifecycle needs including old age.

- **Micro Equity**

Equity investment is playing an increasingly important role in providing financing for microfinance institutions (MFIs) around the world. In India, debt and donations have traditionally supplied the bulk of financing for MFIs, but over the past year and a half, equity investment in the microfinance sector has risen dramatically. Due to recent regulatory changes and the strong growth of the overall microfinance sector in India, the demand for equity financing is likely to rise even further in future years.

Finally, there is a ray of hope for small micro-lenders in Andhra Pradesh. A year ago Finance Minister Pranab Mukherjee had proposed creation of a dedicated fund to provide equity to assist small microfinance institutions in expanding operations.

- **Credit unions**

  Credit unions are not-for-profit organizations that exist to serve their members. Like banks, **credit unions** accept deposits, make loans and provide a wide array of other financial services. But as member-owned and cooperative institutions, credit unions provide a safe place to save and borrow at reasonable rates.

- **Micro Finace Secuization :**

  A securitization is essentially a bundled group of assets with relatively predictable future cash flows that are transferred off the books of the original holder to an independent entity known as a special purpose vehicle (SPV). The SPV sells the rights to the future cash flows in the form of a security which provides the seller with a decreased risk profile and an influx of immediate capital at a relatively low cost; and they provide the purchaser with exposure to the desired market and cash flows over time.. As standardized instruments, they are tradeable and are typically sold to third parties such as banks, mutual funds and insurance companies.

Types of microfinance institutions in India

Joint Liability Group (JLG)

Joint Liability Group can be explained as the informal group consists of 4-10 individuals who try to avail loans against mutual guarantee from banks for the purpose of agricultural and allied activities. This category generally consists of tenants, farmers and other rural workers. They work primarily for lending purposes, although they also offer the savings facility. In this type of institution every individual of a borrowing group is equally liable for the credit.This kind of institution is simple in nature and requires little or no financial administration

Self Help Group (SHG)

Self Help Group is a type of formal or informal group consisting of small entrepreneurs with similar kind of socio-economic backgrounds. Such individuals temporarily come together and generate a common fund to meet the emergency needs of their business. These groups are generally non-profit organizations. The group assumes the responsibility of debt recovery. The advantage of this micro-lending system is that there is no need for collateral. Interest rates are also generally low and fixed especially for women.In addition various tie-ups of banks with SHGs have been implemented for the hope of better financial inclusion in rural areas.

Characteristics of SHG

- Small group of poor (10-20)preferably women
- Similar socio –economic background
- United for common cause
- No need for registration
- Group functioning /Discipline
- Savings/Borrowing/Lending

One of the most important ones is **NABARD** SHG linkage program where many self-help groups can borrow credit from bank once they successfully present a track record of regular repayments of their borrowers. It has been very successful especially in Andhra Pradesh, Tamil Nadu, Kerala and Karnataka and during the year of 2005-06. These states received approximately 60% of SGH linkage credit .

Small Industries Development Bank of India, is an independent financial institution aimed to aid the. Currently the ownership is held by 34 Government of India owned / controlled institutions. Beginning as a refinancing agency to banks and state level financial institutions for their credit to small industries, it has expanded its activities, including direct credit to the SME through 100 branches in all m growth and development of micro, small and medium-scale enterprises (MSME) in India.

Besides, it has been playing the development role in several ways such as support to micro-finance institutions for capacity building and onlending. Recently it has opened seven branches christened as Micro Finance branches, aimed especially at dispensing loans up to 5 lakh. On 28 August 2017, Mohammad Mustafa became the new Chairman and Managing Director of SIDBI

The Grameen Bank Model

Grameen Model was introduced by the Nobel laureate Prof. Muhammad Yunus in Bangladesh during 1970s. It has been widely adopted in India in the form of Regional Rural Banks (RRB). The goal of this system has been the overall development of the rural economy which generally consists of financially backward classes. But this model has not been fully successful in India as rural credit and system of recovery are a real problem. Huge amount of non-performing assets also led to failure of these regional banks Compared to this model Self Help Groups have been more successful as they are more suited to the population density of India and far more sustainable

Rural Cooperatives

Rural Cooperatives in India were set up during the time of independence by the government. They used the mechanism to pool the resources of people with relatively small means and provide financial services. Due to their complex monitoring structure, their success has been limited. In addition, this system only catered to the credit-worthy individuals of rural areas, not covering a large part of the country's financially backward section.

Swarnajayanti Gram Swarojgar Yojana (SGSY)

Swarnajayanti Gram Swarojgar Yojana (SGSY) is an initiative launched by the Government of India to provide sustainable income to poorest of the poor people living in rural & urban areas of the country. The scheme was launched on April 1, 1999.

The SGSY(Swarnajayanti Gram Swarojgar Yojana) aims at providing self-employment to villagers through the establishment of self-help groups. Activity clusters are established based on the aptitude and skill of the people which are nurtured to their maximum potential. Funds are provided by NGOs, banks and financial institutions.

Working of the scheme

The SHGs created may have a varying number of members based on the terrain and physical abilities of the members. It goes through three stages of creation:

- Group formation
- Capital formation through the revolving fund and skill development and
- Taking up of economic activity for skill generation.

POVERTY AND NEED OF MICRO FINANCE

- **Lifecycle Needs**: such as weddings, funerals, childbirth, education, home building, widowhood and old age.
- **Personal Emergencies:** such as sickness, injury, unemployment, theft, harassment or death.
- **Disasters:** such as fires, floods, cyclones and man-made events like war or bulldozing of dwellings.
- **Investment Opportunities**: expanding a business, buying land or equipment, improving housing, securing a job, etc.

GENDER ISSUES

Microfinance generally agree that women should be the primary focus of service delivery. Evidence shows that they are less likely to default on their loans than men.

Microfinance's emphasis on female-oriented lending is the subject of controversy, as it is claimed that microfinance improves the status of women through an alleviation of poverty. It is argued that by providing women with initial capital, they will be able to support themselves independent of men, in a manner which would encourage sustainable growth of enterprise and eventual self-sufficiency. This claim has yet to be proven in any substantial form.

Benefits

- Microfinancing produces many benefits for poverty stricken, or low- income households. One of the benefits is that it is very accessible.
- Banks today simply won't extend loans to those with little to no assets, and generally don't engage in small size loans typically associated with microfinancing. Through microfinancing small loans are produced and accessible.

- Microfinancing is based on the philosophy that even small amounts of credit can help end the cycle of poverty.
- Another benefit produced from the microfinancing initiative is that it presents opportunities, such as extending education and jobs.
- Families receiving microfinancing are less likely to pull their children out of school for economic reasons.
- As well, in relation to employment, people are more likely to open small businesses that will aid the creation of new jobs.

Limitations

There are also many challenges within microfinance initiatives which may be social or financial.

- Here, more articulate and better-off community members may cheat poorer or less-educated neighbours. This may occur intentionally or inadvertently through loosely run organizations. As a result, many microfinance initiatives require a large amount of social capital or trust in order to work effectively.
- The ability of poorer people to save may also fluctuate over time as unexpected costs may take priority which could result in them being able to save little or nothing some weeks. Rates of inflation may cause funds to lose their value, thus financially harming the saver

Growth of Microfinance Volume Worldwide