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Foundations of

Accounting and Finance

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ii Editorial Team Prof. K. Seethapathi IFHE (Deemed-to-be-University), Hyderabad Prof. A. Suresh Babu IFHE (Deemed-to-be-University), Hyderabad Prof. D. Satish IFHE (Deemed-to-be-University), Hyderabad Dr. Naseem Ahamed IFHE (Deemed-to-be-University), Hyderabad Dr. K. Rajya Lakshmi IFHE (Deemed-to-be-University), Hyderabad Prof. U. L. Sunitha IFHE (Deemed-to-be-University), Hyderabad Content Development Team Prof. C. Padmavathi Prof. Dharani IFHE (Deemed-to-be-University), Hyderabad IFHE (Deemed-to-be-University), Hyderabad Prof. U. L. Sunitha Dr. K. Rajya Lakshmi IFHE (Deemed-to-be-University), Hyderabad IFHE (Deemed-to-be-University), Hyderabad Prof. M. Kirthika Dr. M. R. Senapathy Academic Associate, ISB IFHE (Deemed-to-be-University), Hyderabad Proofreading, Language Editing and Layout Team Ms. Jayashree Murthy Dr. Nirmala IFHE (Deemed-to-be-University), Hyderabad IFHE (Deemed-to-be-University), Hyderabad Mr. Prasad Sistla Mr. Venkateswarlu IFHE (Deemed-to-be-University), Hyderabad IFHE (Deemed-to-be-University), Hyderabad © The ICFAI Foundation for Higher Education (IFHE), Hyderabad.

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Foundation for Higher Education (IFHE), Hyderabad welcomes suggestions from students for improvement in future editions. Our E-mail id: cwfeedback@icfaiuniversity.in Centre for Distance and Online Education (CDOE) The ICFAI Foundation for Higher Education (Deemed-to-be-University Under Section 3 of UGC Act, 1956) Donthanapally, Shankarapalli Road, Hyderabad- 501203.

iii BLOCK IV: FINANCIAL MANAGEMENT Financial Management deals with financial decision making on the basis of the data derived from financial accounting and cost accounting. A Finance Manager in today's world undertakes several functions such as procurement of funds, allocation of funds, management of working capital needs, financing of international projects etc.

Hence, it is imperative for a finance manager to be well-versed with the basic concepts of financial management, environment of corporate finance, financial system – both domestic and international,

time value of money, sources of long-term finance and working capital management. This block consists of six units which give an overview of the above mentioned concepts. Unit 9 Introduction to Financial Management discusses the nature and objectives of financial management, interface of financial function with other functional areas, and the environment of corporate finance.

Unit 10

Financial Management Process describes the process of financial management in government, government entities, corporates and by individuals. The concept of Public Financial Management with emphasis on budgetary and non-budgetary activities and the functions of Niti Aayog are outlined in the unit. The various sources and uses of funds by corporates are also illustrated. The unit covers the goals of personal financial management and sources and uses of funds by individuals.

Unit 11 Financial System – Indian and International Scenario gives an overview of the Indian and International Financial System and its components - financial markets, financial institutions and financial instruments.

Unit 12 Time Value of Money

outlines methods of compounding and discounting, future value of a single flow, future value of multiple flows and future value of annuity. It also covers the present value of a single flow, present value of uneven multiple flows and present value of annuity.

Unit 13 Sources of Long term and Short term Finance outlines the need for long-term and

short term finance and the different types of sources. The

unit also covers issuing procedure of various securities. It discusses the need for working capital, various components of current assets and current liabilities and various factors affecting composition of working capital. Besides, the unit also discusses estimation of a firm's working capital needs using operating cycle.

Unit 14 Basics of International Trade and Finance discusses the need for international finance, the meaning and implications of globalization and the benefits and costs of integration of financial markets.

The unit also explains the export and import procedure while outlining regulatory requirements to be satisfied in this process.

The

highlights of the Foreign Trade Policy (2015-2020) are also covered.

iv The block units have been revised to incorporate the latest exhibits and addition to content where necessary. Latest examples have been inserted to provide the learner better understanding of the concept and its applications. The impact of the COVID-19 Pandemic on the Financial system was captured in the various exhibits, while the latest budget 2021-22 figures have been added to enhance the understanding of the learner. New concepts such as SEBI's proposal for T+1 trading cycle, Foreign Trade Policy proposal for 2021-2026 and Alternate Minimum Tax (AMT) are added.

Unit 9 Introduction to Financial Management Structure 9.1 Introduction 9.2 Objectives 9.3 Difference between Accounting and Finance 9.4 Nature and Objectives of Financial Management 9.5 Scope of

Financial

Management 9.6

Summary 9.7 Glossary 9.8 Self-Assessment Test 9.9

Suggested Readings/Reference Material 9.10 Answers to Check Your Progress Questions 9.1

Introduction

Financial management

has tremendous importance in the modern economic world.

At the same time, it is becoming complex day-by-day. Finance managers who were hitherto confined to national markets are now looking towards international markets for their financing and investment activities. Financial management deals with financial planning and decision-making and includes all the tools and analysis for planning and decision-making. It is not confined to profit making alone. The common thread running through all the decisions taken by managers is money. There is hardly any manager working in an organization to which money does not matter. Quite often, businesses are confronted with situations where decisions, which have important financial implications, need to be taken. It may be R&D, expansion of business, replacement of equipment, advertising or raising of funds domestically or internationally.

This unit is intended to provide an overview of the financial management, its nature and objectives. The objectives revolve around the functions that a finance manager performs. The unit also explores the scope of financial management by understanding the linkages that this discipline has with other disciplines, especially accountancy as most of the financial data is taken from the accounting records. 9.2

Objectives After reading through the unit, the student should be able to: ?

Differentiate between accounting and finance ?

Understand the nature and objectives of financial management ? Define the role of a finance manager ? Discuss the interface between finance and other functions

Block IV: Financial Management 2 9.3

Difference between Accounting and Finance In the previous units, we have learnt about the accounting process. The accounting process comprises of recording, classifying, summarizing, and interpreting the financial information in a business. Accounting is done with the twin objectives of ascertaining the profit or loss of the business after a specific period and evaluating the financial position of the business on a specific day. Accounting information has frequently been criticized as being historical and irrelevant for decision making. However, the activities performed by a Finance Manager are much broader in scope than that of an Accountant or Accounts Manager. 9.3.1 Financial Management What is Financial Management?

Finance can be defined as the science and art of managing money. At the personal level, finance is concerned with individuals' decisions about how much of their earnings they spend, how much they save, and how they invest their savings. In a business context, finance involves the same types of decisions: how firms raise money from investors, how firms invest money in an attempt to earn a profit, and how they decide whether to reinvest profits in the business or distribute them back to investors. Financial management is an integral part of management. All organizations, legal entities, individuals, government/quasi government entities are required to manage their finances effectively and efficiently. This necessitates an understanding of the subject of Financial Management.

Financial Management Decisions We have to answer the following questions to understand the financial management decisions. 1. What type of long-term investment should you take for your business? 2. Where will you find the funds to finance for your long-term investment for your business? 3. How will you manage day-to-day activities of your business? Capital Budgeting: The first question concerns the firm's long-term investments. The process of planning and managing a firm's long-term investments is called capital budgeting. In capital budgeting, the financial manager tries to identify investment opportunities that are worth more to the firm than they cost to acquire. Loosely speaking, this means that the value of the cash flow generated by an asset exceeds the cost of that asset. Evaluating the size, timing, and risk of future cash flows is the essence of capital budgeting.

Unit 9: Introduction to Financial Management 3 Capital Structure: The second question for the financial manager concerns ways in which the firm obtains and manages the long-term financing it needs to support its long-term investments. A firm's capital structure (or financial structure) is the specific mixture of long-term debt and equity the firm uses to finance its operations. The financial manager has two concerns in this area. First, how much should the firm borrow? That is, what mixture of debt and equity is best? The mixture chosen will affect both the risk and the value of the firm. Second, what are the least expensive sources of funds for the firm? Working Capital Management: The third question concerns working capital management. The term working capital refers to a firm's short-term assets, such as inventory, and its short-term liabilities, such as money owed to suppliers. Managing the firm's working capital is a day-to-day activity that ensures that the firm has sufficient resources to continue its operations and avoid costly interruptions. This involves a number of activities related to the firm's receipt and disbursement of cash. Some questions about working capital that must be answered are the following: (1) How much cash and inventory should we keep on hand? (2) Should we sell on credit? If so, what terms will we offer, and to whom will we extend them? (3) How will we obtain any needed short-term financing? Will we purchase on credit or will we borrow in the short term and pay cash? If we borrow in the short term, how and where should we do it? These are just a small sample of the issues that arise in managing a firm's working capital.

Let us look at the following examples: Example 9.1 Kae Capital is a sector agnostic fund and invests in companies, which bring about innovative solutions for the existing gaps in the markets, focusing investing in Innovation, Leadership and Growth.

Kae Capital is a destination for early stage companies to acquire capital for growth. In September 2020, the company participated in a Series A round funding of Hippo Video, a video customer experience platform. In July, 2021 it invested in Zetwerk, a contract manufacturer of capital and consumer goods 1. Sasha Mirchandani is the Managing Director and Founder of Kae Capital. Example 9.2

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MATCHING BLOCK 3/173

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Central Public Sector Enterprises ETF runs a concentrated portfolio with

only few stocks. The portfolio of this ETF (Exchange Traded Fund) is mainly focused on shares in

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energy and oil sector. Nippon Life India Asset Management company (formerly known as

the

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Reliance Nippon Life Asset Management) is managing the CPSE-ETF on

behalf of the government. The 1 <https://www.livemint.com/companies/news/zetwerk-nearly-triples-revenues-to-rs-949-crore-in-fy21-11625656599690.html>

Block IV: Financial Management 4 CPSE-ETF tracks the shares of six PSUs (Public Sector Undertakings) -

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ONGC, NTPC, Coal India, IOC, REC, PFC, Bharat Electronics, Oil India, NBCC India, NLC India and SJVN.

being given to Anchor Investors. In January, 2020 CPSE-ETF announced a fund offer to retail investors worth ₹ 10,000 crore.

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The proceeds from this offer will enable the Government to meet its disinvestment target of ₹ 1.05 lakh crore 2 .

Example 9.3 Nestle India Limited posted a net profit of ₹ 602 crores for quarter ended March 31, 2021, which was a 14.6% year-on-year growth in net profit. Post this, the Board of Directors of the company, on April 22, 2021, announced an interim dividend of ₹ 25 per share. The face value of the share is ₹ 10. This would result in a cash outlay of ₹ 241 crore 3

The above examples raise the following issues: 1. An Investment Company is providing long-term funding to startup companies. 2. A Mutual Fund is mobilizing funds from the investing public. 3. The Government of India disinvestment plan mopped up huge funds to the government. 4. A listed company announced dividend to its shareholders. All these activities are related to one or the other forms of financial management at work. In the light of above, we understand that Financial Management refers to the planning, organizing, directing, and controlling of the financial activities of a business such as procurement and utilization of funds. It also involves applying the general management principles to financial resources of the organization. Financial Management is thus concerned with the three broad areas of financial decision making which are as follows: ? Capital Budgeting (Investing Decision) ? Capital Structure (Financing Decision) ? Dividend Decisions 9.3.2 Accounting and Financial Management The accounting and finance functions are closely inter-linked and are forms of managing money in the business. Financial Accounting deals with the recording of financial transactions of an entity and generating financial statements that disclose the result and the financial position of the business. The information 2 <https://www.livemint.com/market/stock-market-news/>

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govt-plans-to-garner-rs-10-000- cr-from-7th-tranche-of-cpse-etf-11579784581897.

html 3 <https://economictimes.indiatimes.com/>

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markets/stocks/earnings/nestle-q1-results-net- profit-rises-15-yoy-to-rs-602-crore-beats-estimates/

articleshow/82162202.cms
Unit 9: Introduction to Financial Management 5

derived from the financial accounting database forms the raw material for financial decision making by a finance manager. Thus, very often the proximity of the two subjects leads one to assume that they are identical. However, the two subjects widely differ with regard to their scope, objective, purpose, and methodology. The differences between Accounting and Finance are as discussed below: 1. Scope: Accounting is geared towards preparation of financial statements, whereas financial management is oriented towards using the financial information for decision-making. 2. Goal/Objective: Accounting gives information on the performance of the organization during a past period. It is thus to be regarded as a storekeeping function. The principal objective of financial management is value maximization. In the words of Gitman: "The accountant's role is to provide consistently developed and easily interpreted data about the firm's past, present and future operations. The financial manager uses this data, either in raw form or after certain adjustments and analyses, as an important input to the decision making process." 3. Methodology: Accounting is based on the accrual system which recognizes incomes and expenses on the basis of the period to which they belong to, irrespective of whether cash has been paid or not or received or not. On the other hand, the finance manager is more inclined towards cash flows associated with a financial decision. He is interested in the magnitude, timing and risk involved in generating cash flows. 4. Time Period: Accounting deals with historical or past data. It gives information about what has happened; hence, it is information of facts. On the other hand, financial management involves decisions for future events under conditions of uncertainty and risk. 9.4 Nature and Objectives of Financial Management One participant in a course titled, 'Finance for Non-Finance Executives' made a very interesting observation during the discussion. He said, "There are no executive development programs titled 'Production Management for Non- Production Executives' or 'Marketing Management for Non-Marketing Executives' and so on. Then how is it that

books and Executive Development Programs titled 'Finance for Non-Finance Executives' are so popular among managers of all functions like marketing, production, personnel, R&D, etc.?" The answer is very simple. The common thread running through all the decisions taken by the various managers is money and there is hardly any manager working in any organization to whom money does not matter. To illustrate this point, let us consider the following instances.

Block IV: Financial Management 6

The R&D manager has to justify the money spent on research by coming up with new products and processes which would help to reduce costs and increase revenue. If the R&D department is like a bottomless pit only

that is

swallowing more and more money but not giving any positive results in return, then the management would have no choice but to close it. No commercial entity runs an R&D department to conduct basic research

for no purpose. Likewise, the materials manager should be aware that the

inventory of different items in stores is nothing but money in the shape of inventory. He should make efforts to reduce inventory so that the funds released could be put to more productive use. At the same time, he should also ensure that

the

inventory of materials does not reach such a low level as to interrupt the production process. He has to achieve the right balance between too much and too little inventory. This is called the 'liquidity-profitability trade-off' about which you will read more

in the unit on

sources of long term and short term finance.

The same is true with regard to every activity in an organization. The results of all activities in an organization are reflected in the financial statements in rupees. The Finance Manager, as his very designation implies, should be involved in all financial matters of the organization since almost all activities in the organization have financial implications. It would therefore not be inaccurate to say that the Finance Manager is involved in most decisions of the organization. Let us try to understand what financial management is by examining what the Finance Manager does and with what objectives. Let us examine the objectives sought to be achieved by

a Finance Manager. Maximizing the wealth of the owners by increasing the value of the firm:

Suppose he manages to make available the required funds at an acceptable cost and that the funds are suitably invested and that everything goes according to plan because of the effective control measures employed by him. If the firm is a commercial or profit-seeking firm, then the results of good performance are reflected in the profits the firm earns. How are the profits utilized? They are partly distributed among the owners as dividends and partly recycled into the operations of the firm. As this process continues over a period of time, the value of the firm increases for the simple reason that the firm is able to generate attractive surpluses from operations. If the shares of a firm are traded on the stock exchange, the good performance of the firm is reflected in the price at which its shares are traded. When the firm's shares attract a good price, the owners or shareholders are better off because they would realize much more than what they had invested. Their wealth increases. Therefore, we can see that as a result of good financial management, the value of the company to the owners (shareholders) increases, thereby increasing their wealth. So, we can say that the objective of a Finance Manager is to increase or maximize the wealth of the

Throughout the study material, the terms 'firm' and 'company' have been used interchangeably.

Unit 9: Introduction to Financial Management 7

the

owners by increasing the value of the firm, which is reflected in its Earnings Per Share (EPS) and the market price of its shares.

Let's look at the example of how Bajaj Finance succeeded in creating wealth for its shareholders by emerging as a strong contender to SBI, the largest Public Sector Bank. Exhibit 9.1:

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Bajaj Finance surpasses SBI in Market Capitalization On 24th August 2021, the shares of Bajaj Finance traded 3.40 % higher at ₹ 6,983.35 a share on BSE, taking its market cap to ₹ 4.22 lakh crore, surpassing that of SBI's ₹ 3.71 lakh crore as the latter's shares traded up only by 1.56% at ₹ 415.70 a share. This is not the first time that this non-banking finance firm overtook India's biggest lender by assets. Bajaj Finance, on 1 st October 2019, was trading on BSE at ₹3,992.20, taking its market cap to ₹2.32 lakh crore. On that day the price of SBI, fell to ₹254.55 a share, bringing down its market cap to ₹2.28 lakh crore, falling behind Bajaj Finance. At that time Bajaj had a total loan book of ₹1.25 lakh crore, while SBI's stood at ₹22.40 lakh crore. On 17 th Feb 2020, and again on 22 nd June 2020 Bajaj Finance pipped SBI in market capitalisation.

One major advantage for Bajaj Finance was that its share price was higher than that of SBI. This was possible as Bajaj Finance was consistently posting enviable earnings, SBI couldn't. Also, Bajaj Finance

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has cracked the code in consumer lending. Despite most of its loans being unsecured, for its mastery in the art of pricing risk, asset quality metrics of Bajaj

Finance remained incredible.

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The consistent and far better earnings of Bajaj have made the share highly palatable to investors.

Source: <https://icfaibytes.in/2021/09/02/bajaj-finance-surpasses-sbi-in-market-cap/>

Efficient utilization of resources:

In the case of public sector companies, until recently the only objective was to increase the economic welfare of

the society and the nation at large. This objective was achieved by ensuring availability of essential goods and services to all citizens in all corners of the country, uniform development of all regions in the country, providing employment opportunities, investing in projects with long gestation periods where private investment may not be forthcoming and investing in import-substitution industries, etc. But now the public sector has also come to realize that they have to perform in order to exist and that its products/services will not be subsidized any longer by the government. Public Sector Undertakings (PSUs) are now going in for disinvestment and privatization for increased efficiency. 5

Earnings per share refer to the earnings of equity shareholders after all other obligations of the firm have been met.

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Facing new financial challenges: Financial Management, irrespective of whether it is in the context of public sector undertakings or for private sector institutions, has been evolving over the years. The discipline, which traditionally dealt with functions such as procurement of funds, efficient allocation of funds and maximization of firms' value, has over the years encompassed several new elements such as portfolio management, risk management, corporate or strategic finance, etc. The field is constantly evolving. In such a scenario, there are bound to be diverse challenges that are faced by the profession.

Check Your Progress – 1 1. Which of the following is not a part of

financial management? a.

Dividend decisions b. Financing decisions c. Working Capital decisions d. Investment decisions e. Preparation of financial statements 2.

The objective of financial management to increase the wealth of the shareholders means to a. Increase the physical assets owned by the firm b. Increase the market value of the shares of the firm c. Increase the current assets of the firm d. Increase the cash balance of the company e. Increase the total number of outstanding shares of the company 3.

In November 20xx, a telecom company acquired media giant Time Warner for USD109 billion including net liabilities. What type of financial management decision can this be categorized into? a. Dividend decisions b. Financing decisions c. Working Capital decisions d. Investment decisions e. Liquidity decision 4. What was the financial objective of public sector companies in the past? a. Increase profitability b. Improve the conditions of work for employees c. Employment generation d. Increase the wealth of the society e. Increase the wealth of its shareholders

Unit 9: Introduction to

Financial Management 9 5.

Which of the following is not a function of the

finance manager? a. Mobilizing funds b. Risk-return trade-off c. Deployment of funds d. Control over the uses of funds e. Recording of

financial information

Activity 9.1 1. There is a paradigm shift in the objectives of financial management from looking towards profit maximization to value maximization. Discuss the reasons for this shift. 2. Though the disciplines of accounting and financial management are different in many aspects, both deal with money and tracking numbers. However, experts agree that the disciplines are more than tracking numbers and can be used to reduce expenditure and increase revenue. Describe any two areas where accounting and financial management can be employed for reducing expenditure. 9.5 Scope of Financial Management

The Finance Manager is engaged in the following activities: 9.5.1 Mobilization of Funds The Finance Manager needs to plan for and mobilize the required funds

at an acceptable cost from various sources as and when their requirement arises.

This decision is called the Financing Decision. This calls for liaising with banks and financial institutions. The Finance Manager deals with merchant banking agencies for procuring funds from the public through issue of shares, debentures and inviting the public to subscribe to its fixed deposits. While raising funds from various sources, he needs to weigh many considerations like the cost of the funds in the form of interest/dividend and the cost of public issue in the case of shares and debentures, the length of time for which funds would be available,

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etc. Banks and other financial institutions, which give short-term and long-term loans generally, lay down some conditions. These conditions are aimed at ensuring the safety of the loans they give and contain provisions restricting the freedom of the borrower to raise loans from other sources. Therefore, the Finance Manager would try to balance the advantages of having funds available with the costs and the loss of flexibility arising from the restrictive provisions of the loan contract. Let us take a look at a real life example: XYZ Limited, a well-known company in computer training, software development, information systems, consultancy, etc., is undertaking a modernization cum expansion

scheme, which envisages addition of new services, product lines and up gradation of existing systems. The cost of this expansion cum modernization program is estimated at ` 3,578 lakhs, which is going to be mobilized as follows 6 as per the prospectus of the company. Particulars ` in lakh Public issue of equity shares including premium 1,804 Term loan – ICICI 130 Leasing – ICICI – Others 125 75 Deferred payment guarantee 99 Internal accruals 1,345 3,578 9.5.2 Deployment of Funds There are always many competing needs for the allocation of funds. In consultation with the managers of various departments such as production, marketing, personnel, R&D, and the top management, the Finance Manager decides on the manner of deployment of funds in various assets such as land, buildings, machinery, materials, etc. Sometimes the managers of the various departments named above constitute an 'Investment Committee' and appraise an investment proposal along the marketing, technical and financial dimensions. The Finance Manager appraises the proposal along the financial dimensions to determine its worthiness in relation to the investment involved. This decision called the 'Investment Decision' constitutes one of the core activities of the Finance Manager. The funds mobilized through various sources by XYZ are proposed to be deployed as follows, as indicated in the prospectus of the company. 6 The various sources of finance will be discussed in detail in the chapter on Sources of Long-Term and Short Term Finance.

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Particulars ` in lakh Buildings 985 Computers & Accessories 941 Plant & Machinery 116 Infrastructure 213 Normal Capital Expenditure 241 Repayment of Loans 283 Increase in Working Capital 799 3,578 9.5.3 Working Capital Management - A Complexity of Liquidity and Profitability Management

Working capital management involves not only managing different components of current assets, but also managing the current liabilities; or to be more precise, financing aspect of current assets. Working capital management also involves managing a proper balance between liquidity and profitability. The financial manager has to maintain efficiently the level of current assets over and above the level of current liabilities to avoid dangers of illiquidity and insolvency. In some cases, more investment in current assets leads to poor profitability and vice-versa. Hence, the working capital management is a complexity of liquidity and profitability.

Working capital

management is influenced not only by the attitude of company toward risk, but it is also affected by the adequate level of current assets desired by the firm.

Arriving at an optimum level of current assets involves balancing the liquidity and profitability criteria and depends on the mode of financing the current assets chosen by the firm. These decisions are called 'Working Capital Management'. 9.5.4

Utilization of Company's Profits after Tax

A financial manager has basically two options on the utilization of company's profits after tax, viz. either re-invest the earnings by retaining them or allocate the same to the shareholders as dividends. Firms may go for the first option if they are in need of funds to fund their long-term projects. However, this option might be appropriate only if such projects have enough growth potential and can generate substantial profits. On the other hand, if the firms go in for the second option of paying cash dividends from the profits after tax, it will result in maximization of the shareholders' wealth. But it is subject to availability of cash for payment of dividends. Thus, the returns those accrue to the shareholders either by way of the dividend receipts or by capital gains, are affected by the dividend policies of the firms.

Exhibit 9.2 below shows an example of how the Indian Companies have been resorting to high dividend payments even in COVID-19 situation.

Block IV: Financial Management 12 Exhibit 9.2: Generous Dividend Payments by Indian Companies Indian companies continued to pay good dividends to their shareholders in 2020-21 and in the previous three years, even though their business operations were hampered by the Pandemic COVID-19 and the resultant lockdown. A study by Mint revealed that the dividend payout ratio of 42 companies that were part of Nifty increased to 38.1% in 2020-21 as against 37.3% in 2019-20. This ratio was 30.7% in 2018-19, 33.7% in 2017-18 and 49.4% in 2016-17. However, the dividend payout ratio of 398 firms, mostly mid-sized firms reduced indicating that the impact of the Pandemic was more severely felt on the mid-sized companies than on the large companies. The reasons cited for the continued payments of higher dividends were: 1. The COVID 19 Pandemic has created an uncertain investment climate. The lack of demand for investment options have made companies divert the surplus to dividend payments 2 A more substantial reason was the positive impact of the change in the treatment of dividend from a tax perspective, especially post the abolition of dividend distribution tax (DDT), resulting in dividends being taxed in the hands of the investor. 3. The underlying reason as spelt out by Harsh Upadhyay, the Chief Investment Officer in the equity division of Kotak Mahindra Asset Management Company Limited, is that these companies could generate increased revenues and profits. He opined that bigger companies fared better in managing their costs during the Pandemic, thereby translating into higher profits Source: <https://www.livemint.com/market/stock-market-news/dividend-payouts-of-nifty-firms-climb-to-4-year-high-11624214937522.html>, June 2021 9.5.5

Other Functions Control over the Use of Funds After deciding on projects and proposals in which the funds are to be invested and after procuring them, the Finance Manager has the responsibility to continuously monitor their use in order to ensure that the procurement and deployment of funds proceeds according to plan. This task of the Finance Manager is called Financial Control. The Finance Manager sends frequent reports to the Managing Director. These reports contain information in the form of data regarding the extent to which procurement and deployment of funds is proceeding according to plan. For example, the reports would inform the management regarding the extent to which credit sanctioned by banks for the day-to-day use of the firm (working capital) has been utilized and how much more can be borrowed. It would also contain information on the quantum of money that is due to the firm from various customers and how much the firm is due to

its suppliers. The report would also contain information on the funds

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required at different points of time in the future and the availability of funds from various sources including those available out of any surpluses generated internally. He would also be reporting to the top management about the performance of individual departments within the organization. All such reports are called 'Control Reports' and the whole process constitutes 'control' because it helps the management to take timely corrective action to ensure that planned results are achieved.

Exhibit 9.3 given below describes

how finance leaders need to relook at their roles and responsibilities in changing times. Exhibit 9.3: Roles and Responsibilities of Finance leaders in New Operating Environment Ernst & Young (EY) conducted a survey of more than 1,000 CFOs (Chief Financial Officers) and Financial controllers operating in more than 25 countries. The survey was to gauge how the finance leaders perceive the change in their roles and responsibilities amid the Pandemic and global economic and political disruptions in the pandemic has created. One major area was the influence of technology in the delivery of financial services. The survey results point that: ? Technology may replace more than 50% of the tasks currently being taken up these leaders ? Around 54% of the surveyed expressed the opinion that blockchain based systems will strengthen finance ? There was a strong voice on the risks associated with applying artificial intelligence in finance and reporting with 63% of the respondents expressing doubt on the security of using this technology. The respondents felt that enhanced reporting and governance practices can reduce the risks associated with technology. The survey also brought to light the fact that investors or stakeholders view finance leaders as stewards of long term value creation in the organization. As such, they are looking toward finance leaders to provide them with forward looking financial analysis, forecasts, insights on non-financial factors such as ESG (Environment, Sustainability and Governance) reporting etc. In the words of Tim Gordon, EY Global Financial Accounting Advisory Services Leader, "Finance leaders should rethink the role that reporting is expected to play in helping to tell the story of the value that the enterprise creates. If finance fails to play a central role in meeting these changing expectations, reporting could become increasingly irrelevant." Source: Konstantinos Makrygiannis. Finance leaders rethink roles and responsibilities as new operating reality sets in. EY, February 2021 https://www.ey.com/en_gl/news/2021/02/finance-leaders-rethink-roles-and-responsibilities-as-new-operating-reality-sets-in

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Risk-Return Trade-off While making the decisions regarding investment and financing, the Finance Manager seeks to achieve the right balance between risk and return. If the firm borrows heavily to finance its operations, then the surpluses generated out of operations would be utilized to 'service the debt' in the form of interest and principal payments. The surplus or profit available to the owners would be reduced because of the heavy 'debt-servicing'. If things do not work out as planned and the firm is unable to meet its obligations, the company is even exposed to the risk of insolvency. Similarly, the various investment opportunities have a certain amount of risk associated with the return and also the time the return would materialize. The finance manager has to decide whether the opportunity is worth more than its cost and whether the additional burden of debt can safely be borne. In fact, decision-making in all areas of management, including financial management involves the trade-off between risk and return. Treasury Operations Short-term fund management has become more sophisticated. Finance managers could make speculative gains by anticipating interest rate movements. Foreign Exchange Finance Managers will have to weigh the costs and benefits of transacting in foreign exchange, particularly now

as

the economies are going global and the future value of the currency has become difficult to predict. Financial Structuring An optimum mix between debt and equity will be essential. Firms need to tailor financial instruments to suit their needs as also those of investors. Pricing of new issues is an important task for the Finance Manager's portfolio. Maintaining Share Prices In the premium equity era, firms must ensure that share prices stay healthy.

The

Finance manager needs to devise appropriate dividend and bonus policies. Ensuring Management Control Equity issues at premium means that the management may lose control if it is unable to take up its share entitlements. Strategies to prevent this are vital.

The management of finance function requires managers not only to be well versed with the above activities, but also to be equipped with the changing technology. The IT ecosystem with its constantly evolving dimensions is throwing open challenges to the present day financial manager. The future of financial management can be envisaged as one which is technology enabled.

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Check Your Progress – 2 6.

Which

of the following is not a

function

of

the

finance manager? a. Mobilizing funds. b. Risk-return trade-off c. Deployment of funds d. Control over the uses of funds

e.

Recording of

financial information 7.

The market value of the firm is the result of a. Speculative decisions b. Working capital decisions c. Capital budgeting decisions d.

Trade-off between cost and risk e. Trade-off between risk and return 8.

Finance managers by anticipating interest rate movements could make speculative gains. Which function of financial management is

referred to above? a. Mobilization of funds b. Deployment of funds c. Treasury operations d. Working capital management e. Foreign

exchange management 9. Which function of a finance manager

helps the management to take timely corrective action to ensure that planned results are achieved?

a. Mobilization of funds b. Control over use of funds c. Treasury operations d. Working capital management e. Dividend distribution

10.

Pricing of new issues is an important task for the Finance Manager's portfolio.

Under which function can this activity be segregated into? a. Financial structuring b. Control over use of funds c. Treasury operations

d. Ensuring management control e. Dividend distribution

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Activity 9.2 1.

While making the decisions regarding investment and financing, the Finance Manager seeks to achieve the right balance between risk and return.

Analyze how a finance manager can ensure this balance. 2. Prior to 1991, the financial manager in India performed in a highly regulated environment. However, with the financial sector reforms introduced in 1991, the economic, regulatory and financial environment in the country underwent a sea change. How do you think the role of finance manager changed due to this transformation?

9.6 Summary ? The Financial goal of any organization, whether in the private sector or

public sector is to maximize the wealth of the shareholders by maximizing the value of the firm. ? The objective of the financial

manager is to increase or maximize the wealth of owners by increasing the value of the firm, which is reflected in its earnings per

share and market value of the firm. ? Functions of the finance manager include mobilization of funds, deployment of funds, control

over the use of funds, and balancing the trade- off between risk and return. ?

The

Financing Decision of a finance manager involves planning for and mobilizing the required funds from various sources at an acceptable cost, as and when their requirement arises. . ?

There are always many competing needs for the allocation of funds. In consultation with the managers of various departments such as production, marketing, personnel, R&D, and the top management, the Finance Manager decides on the manner of deployment of funds in various assets such as land, buildings, machinery, materials, etc., which is referred to as the investment decision.

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Introduction to Financial Management 17 ?

A financial manager has basically two options on the utilization of company's profits after tax, viz. either plough back the earnings by retaining them or distribute the same to the shareholders.

This is known as dividend decision of the firm. ?

Working capital management involves not only managing different components of current assets, but also managing the current liabilities; or to be more precise, financing aspect of current assets. Working capital management also involves managing a proper balance between liquidity and profitability. 9.7

Glossary Accounting comprises of recording, classifying, summarizing, and interpreting the financial information in a business.

Accounting is done with the twin objectives of ascertaining the profit or loss of the business after a specific period and evaluating the financial position of the business on a specific day. Capital Budgeting refers to long term investment decisions that require huge outlay and are irreversible in nature. Capital Structure/Financial Structuring is the appropriate mix of debt and equity that is used in the financing of a business. Control Reports are the reports prepared by the Financial Controller which reports the performance of the individual departments within the organization to the top management. Deployment of Funds denotes allocation of funds among the various departments in an organization. Financial Control is the task of

the Finance Manager to continuously monitor the funds to ensure that the procurement and deployment of funds are proceeding according to plan

Foreign Investment is an investment by a foreign country, normally where the company being invested in is controlled by foreign shareholders. A British firm taking a major stake in an Indian firm can be an example of foreign investment. Financial Management refers to

the planning, organizing, directing, and controlling of the financial activities of a business such as procurement and utilization of funds.

Investment refers to deploying money in some return generating asset. The returns may be in the form of regular income or capital appreciation. Investment may be for a long period or for a short period, depending on the constraints and objectives of the investor.

Limited Liability is used in the context of joint stock companies. It means that liability of the members towards the company's debt and obligations is limited to their initial investment or stake in the ownership. This safeguards the personal assets of the members from liquidation if the company becomes insolvent.

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Liquidity-Profitability Trade -off is the objective of Finance Manager to achieve the right balance between too much and too little inventory.

Public Sector Undertakings (PSUs) are state owned enterprises in India that are either owned by the Central Government or any one or more of State Governments or both.

Return is the gain or loss from an investment over a particular period. Returns may be in the form of income or capital appreciation. Generally, risk and return go hand-in-hand, i.e. more risk gives more return and low risk gives low return.

Risk includes both upside and downside potential, but we are mostly concerned with the downside one. It can be mathematically calculated

87%

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by measuring the standard deviation of the historical returns or average returns

for a particular investment. Trade refers to the transactions of purchase and sale of tangibles. In general, it refers to trading of goods and services, whereas in the investment world, it refers to trading of securities such as bonds or equity stocks.

Treasury Operations deal with the management of an organization's financial resources with the ultimate objective of maintaining a desired level of liquidity and minimizing its operational, financial and reputational risk.

Working Capital Management involves managing the different components of current assets and current liabilities to maintain a balance between liquidity and profitability. 9.8

Self-Assessment Test 1. What is the objective of Financial Management? 2. What are the major roles of a Finance Manager? 3.

How is Finance different from Accounting? 4.

Why should the Finance Manager be conversant with the regulatory environment? 5. What challenges are faced by a Finance Manager in today's changing business scenario? 6. Describe the scope of financial management. 9.9 Suggested Readings/Reference Material 1.

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Answers to Check Your Progress Questions 1. (e) Preparation of financial statements Preparation of financial statements is part of financial accounting. Financial management deals with investment, financing, working capital, and dividend decisions. 2. (

b) Increase the market value of

the shares of the firm

The objective of a Finance Manager is to increase or maximize the wealth of the

owners by increasing the value of the firm, which is reflected in its Earnings Per Share (EPS) and

the market price of its shares. 3. (

d) Investment decisions

Investment refers to deploying money into some return generating asset. The returns may be in the form of regular income or capital appreciation. Investment may be for a long period or for a short period, depending on the constraints and objectives of the investor.

4. (

d) Increase the wealth of the society

In the case of public sector companies, until recently the only objective was to increase the wealth of the society and the nation at large. This objective was achieved by ensuring availability of essential goods and services to all citizens in all corners of the country, uniform

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development of all regions in the country, providing employment opportunities, investing in projects with long gestation periods where private investment may not be forthcoming and investing in import- substitution industries, etc. 5. (

d) Data related to cash flows that enable future projections The finance manager is more inclined towards cash flows associated with a financial decision. He is interested in the magnitude, timing and risk involved in generating cash flows. 6. (e) Recording of financial

information Recording of financial information is undertaken by an accountant. A finance manager performs functions that include mobilization of funds, deployment of funds, managing working capital, dividend distribution, control over the use of funds, risk-return trade-off, treasury operations, foreign exchange, financial structuring, maintaining share prices, and ensuring management

control. 7. (e) Trade-off between risk and return

Decision-making in all areas of management, including financial management involves the trade-off between risk and return. 8. (c) Treasury Operations Short-term fund management has become more sophisticated. Finance managers could make speculative gains by anticipating interest rate movements. 9. (

b)
Control over use of funds After deciding on projects and proposals in which the funds are to be invested and after procuring them, the Finance Manager has the responsibility to continuously monitor their use in order to ensure that the procurement and deployment of funds proceeds according to plan. This task of the Finance Manager is called Financial Control and the reports that he generates are called 'Control Reports' and the whole process constitutes 'control' because it helps the management to take timely corrective action to ensure that planned results are achieved. 10. (

a)
Financial Structuring An optimum mix between debt and equity will be essential. Firms need to tailor financial instruments to suit their needs as also those of investors. Pricing of new issues is an important task for the Finance Manager's portfolio.

Unit 10 Financial Management Process Structure 10.1 Introduction 10.2 Objectives 10.3 Flow of Financial Management Process in Government 10.4 Funding in Government Agencies and Undertakings 10.5 Funding Needs of Various types of Entities 10.6 Corporate Financial Management 10.7 Financial Management for Individuals 10.8 Environment of Finance 10.9 Regulatory Framework 10.10 Summary 10.11 Glossary 10.12 Self-Assessment Test 10.13 Suggested Readings/Reference Material 10.14 Answers to Check Your Progress Questions 10.1

Introduction

In the previous unit,
we discussed

the various functions of financial management and its importance in the modern economic world. Financial management is applied not only by individuals or business organizations but also by governments. In addition, government activities and policies have a profound impact on the financial management decisions taken by all entities (individuals & all types of organizations) of the economy. Hence, understanding the flow of financial management process from a government perspective is vital. This unit discusses some of the important issues in public finance such as five-year plans, public finance management, budgetary allocations, sources of finance for government entities, etc. The unit also gives an overview of the corporate and individual financial management process. Emphasizing on corporate financial management, the unit describes the various forms of business organizations and their requirements for finance. The regulatory framework laid down by government within which these organizations take financial decisions is also outlined. 10.2

Objectives After reading through the unit, the student should be able to: ? Outline the
flow of
financial

management process in government structure ? Explain the financial needs of various types of entities

Unit 10: Financial Management Process 23 ? Describe the funding process employed in government agencies and undertakings ? Discuss the concept of corporate financial management ? Gain insight into the basics of personal financial planning ? Elaborate the various forms of business organizations and their financial needs ? State the regulatory framework in India impacting the financial environment of businesses 10.3 Flow of Financial Management Process in Government Financial Management is an effective tool for proper funding and deployment across the board to all entities – individuals, firms of all types and the government. The flow of financial management process in a government can be discussed as follows: 10.3.1 The Inter-connectivity in Financial Management Process Financial Management is the effective and efficient management of funds to achieve the objectives of the organization. It includes planning , organizing, directing and controlling the financial activities such as procurement, allocation and financial control taking into account various risks involved in the process. The four major objectives of financial management are to (i) ensure regular and adequate supply of funds to the organization, (ii) ensure adequate returns to the shareholders, (iii) ensure optimum utilization of funds and (iv) ensure safety on investments made. The government policies and their execution play a pivotal role in financial management of business firms and individuals in general. Direct and indirect taxes, fiscal and monetary policies, trade policy, the scope for external borrowing by individuals and firms, etc., are within the powers of the Central government in our country. 10.3.2 Planning Commission and Five-Year Plans After Independence, the Government felt the importance of developing the country economically; and the first five-year plan was initiated in 1951 with focus on primary sector, and subsequent five-year plans with focus on other areas based on the Government priorities. The Planning Commission was formed in March 1950 based on the recommendations of the Economic Program Committee (EPC). The Planning Commission's objectives were: 1. To assess the material, capital and human resources of the country, including technical personnel, and investigate the possibilities of augmenting those resources which are found to be deficient in relation to the nation's requirement. 2. To formulate a plan for the most effective and balanced utilization of country's resources.

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To define the stages, based on priority, in which the plan should be carried out and propose the allocation of resources for the due completion of each stage. 4. To indicate the factors those tend to retard economic development. 5. To determine the conditions which need to be established for the successful execution of the plan within the prevailing socio-political situation of the country. 6. To determine the nature of the machinery required for securing the successful implementation of each stage of the plan in all its aspects. 7. To appraise from time to time the progress achieved in the execution of each stage of the plan, also recommend the adjustments of policy and measures, which are deemed important vis-a-vis a successful implementation of the plan. 8. To make necessary recommendations from time to time regarding those things which are deemed necessary for facilitating the execution of these plans. The

twelfth five-year plan, which began in 2012 culminated in 2017. Exhibit 10.1 provides a snapshot of the outlay and expenditure under various five-year plans in India. Exhibit 10.1: Five Year plans – Outlay and Expenditure in Centre, State Governments and Union Territories (` in Crores) Source: <https://data.gov.in/catalog/plan-outlay-and-expenditure-centre-states-and-union-territories-five-year-plans,2016>

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However, the Government under the leadership of Prime Minister Sri Narendra Modi has replaced the Planning Commission with Niti Aayog in January 2015. NITI Aayog or National Institution for Transforming India Aayog is, basically, a policy think tank of Government of India and State Governments. Its primary job is to undertake long-term policy, design frameworks, take necessary initiatives for attaining faster development and monitor these activities. In Niti Aayog, the States will take a leading role in policy intervention. Hitherto the Planning Commission had the power to allocate funds to states for attaining regional development. With Niti Aayog in place, the Planning Commission has ceased to exist and the allocation of funds to the states is done by the Finance Ministry's Department of Expenditure in the new dispensation. Niti Aayog is formed with the objective of bringing the states together in the national interest and hence is a platform for furthering cooperative federalism. Niti Aayog operates through two hubs: Hub 1: Team India Hub Hub 2: Knowledge and Innovative Hub Objective of working with the states. It has sub-groups of Chief Ministers on centrally sponsored schemes, skill development and Swachh Bharat mission It also has task forces constituted for raising agricultural productivity and making farming financially lucrative. Objective of evolving as a state of the art resource center. It has reports and best practices on various themes. It compiles data state-wise.

Niti Aayog has also forayed into innovative areas such as accounting reforms in Indian Railways, holistic development of the land, evolving key performance indicators in Health, Education and Water sectors etc. A significant role played by the organization is in implementation and tracking of sustainable development goals in accordance with the Millennium Development Goals of the UN. The following Exhibit 10.2 captures the significant functions that this organization performs: Exhibit 10.2: Functions of Niti Aayog The functions performed by Niti Aayog are: ? To evolve a shared vision of national development priorities sectors and strategies with the active involvement of States in the light of national objectives ? To foster cooperative federalism through structured support initiatives and mechanisms with the States on a continuous basis, recognizing that strong States make a strong nation Contd....

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To develop mechanisms to formulate credible plans at the village level and aggregate these progressively at higher levels of government ? To ensure, on areas that are specifically referred to it, that the interests of national security are incorporated in economic strategy and policy ? To pay special attention to the sections of our society that may be at risk of not benefiting adequately from economic progress ? To design strategic and long-term policy, and program frameworks and initiatives, and monitor their progress and their efficacy. The lessons learnt through monitoring and feedback will be used for making innovative improvements, including necessary mid-course corrections ? To provide advice and encourage partnerships between key stakeholders and national and international like-minded Think tanks, as well as educational and policy research institutions. ? To create a knowledge, innovation and entrepreneurial support system through a collaborative community of national and international experts, practitioners and other partners. ? To offer a platform for resolution of inter-sectoral and inter departmental issues in order to accelerate the implementation of the development agenda. ? To maintain a state-of-the-art Resource Centre, be a repository of research on good governance and best practices in sustainable and equitable development as well as help their dissemination to stakeholders ? To actively monitor and evaluate the implementation of programs and initiatives, including the identification of the needed resources so as to strengthen the probability of success and scope of delivery ? To focus on technology upgradation and capacity building for implementation of programs and initiatives ? To undertake other activities as may be necessary in order to further the execution of the national development agenda, and the objectives mentioned above Source: <http://niti.gov.in/content/functions> 10.3.3

Public Finance Management (PFM) Public Finance Management System (

96%**MATCHING BLOCK 14/173****W**

PFM) is an essential aspect of the institutional framework for an effective state. 7

95%**MATCHING BLOCK 15/173****W**

PFM refers to the set of laws, rules, systems and processes used by sovereign nations (and sub-national governments), to mobilize revenue, allocate public funds, undertake public spending, account for funds and audit results. It 7

Source: <http://www.gsdr.org/professional-dev/public-financial-management/>
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encompasses a broader set of functions than financial management and is commonly conceived as a cycle of six phases-

Policy, Budget Formulation, Budget Approval, Budget Execution, Accounting and External Audit. Public Finance Management (PFM), basically, deals with all aspects of resource mobilization and expenditure management in a government. Just as managing finances is a critical function of management in any organization, public finance management is an essential part of the governance process. One of the important criteria to make the PFM is to make the budgetary activities performance oriented. Finance teams in Government departments and other public bodies have a vital role to play if the government is to deliver the planned public service reform and Finance managers have to play a more central role in the efforts to provide sustainable services at lower cost. This can be possible by strengthening the Treasury and Finance departments and its leadership groups, thus strengthening the financial management capability across government. In recent years, the role of a sound PFM system in achieving the objectives of fiscal discipline, strategic planning and improved service delivery has been receiving increased public attention in India and Government has initiated PFM reform measures to enhance the effectiveness of the PFM system. The Funding Angle In public corporate sector the finance manager has to plan for mobilizing funds from various sources which include funds from the public through issue of shares, debentures, loans from financial institutions such as Banks, Insurance companies, Development financial institutions etc. In case of government bodies, the funding can be through both budgetary and non-budgetary activities. Budgetary Activities "A government budget is an annual financial statement showing item wise estimates of expected revenue and anticipated expenditure during a fiscal year." A detailed process of preparation of annual Budget is undertaken by the Government starting with preparation and presentation of the economic survey in the parliament. There are two Budgets, Railway budget and Union budget. The Railway Budget is presented by the union minister for railways a few days before the Union Budget, which is presented on 28/29 th of February. The Budget is discussed in both houses of Parliament and once approved, becomes a finance bill. Implementation of the various measures proposed in the bill will be initiated by the respective departments. Individual States prepare their budgets and present in their respective assemblies for approval. Budgetary process is estimating the availability of resources and allocating them to various activities based on pre-determined priority. Until the Financial Year 2016-17, there are two budgets (Railway budget and union Budget). From the Financial year 2017-18, the railway budget will be merged with Union Budget.

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In the month of February every year the union Finance minister presents before the Lok Sabha, an estimate of Government's revenue and expenditure for the coming financial year with an objective of combining rapid and balanced economic growth with social equality and economic justice. The various sources of revenue are taxes, fees, interest on loans given to states and dividends from public sector units. The various expenditures are providing goods and services to citizens, infrastructure, internal security, expenditure incurred on defense, staff salaries etc. Budgetary

allocation for various sectors for the financial year 2021-22 in the Union Budget is as shown in Exhibit 10.3. Exhibit 10.3: Budgetary Allocations for Major sectors in 2021-22 Sector Budget Allocation (` Crores) Rural

Development 1,94,633 Agriculture and allied activities 1,48,301 Rural development 79,526 Health care 74,602 Education 93,224 Urban development 54,581 social welfare 48,460 Transport 233083 Defence 347088 Source: Union Budget 2021-22

https://www.indiabudget.gov.in/doc/Budget_at_Glance/bag6.pdf

Non-Budgetary Activities All the expenditures undertaken by the Government are considered as non- budgetary activities if the funds are not routed through consolidated fund of the state, outside the budgetary processes and not accounted for in the budget document. Some of them are 1. Central assistance paid directly to government agencies under various schemes 2. Expenditure by state departments/agencies from collection of user charges 3. Public Private Partnership (PPP) Project: 4. Imputed subsidy cost of Government Loans 5. Imputed subsidy cost of Government Guarantees 6. Imputed value of tax reliefs and exemptions

Unit 10: Financial Management Process 29 10.3.4

NITI Aayog and Allocation of Funds to States National Institution for Transformation of India, also called Niti Ayog aims to foster involvement and participation in the economic policy-making process by the State Governments of India. The Prime Minister is the ex Officio chairman of NITI Aayog and the Governing Council is composed of Chief Ministers of the various states and lieutenant governor of Union territories. As per the report of the 15th Finance Commission (FFC) for the year 2020-21, the share of states in the central taxes for 2021 – 2026 period was recommended to be kept at 41% even though the 14 th finance commission 42% share in central taxes. The adjustment of 1% was to provide for the newly formed union territories of Jammu and Kashmir and Ladakh.

Sources of Finance Available to State Governments Some of the sources of funds available to state governments are tax revenue, non-tax revenue, grants-in-aid from Government of India and state's share of union taxes and duties. The State Governments also raise funds through Long- term bonds for development purposes. The tax revenue is the prominent source of funds for the state governments and this includes sales tax, excise, tax on goods, tax on vehicles, stamp duty, electricity duty, tax on passengers and land revenue, tax on professions, trade, selling and employment, entertainment duty and advertisement, road tax and tourist tax. The non-tax revenue is largely dependent on collection of fee from the consumers for supply of goods and services.

Check Your Progress – 1 1.

Which of the following is not an objective of Financial Management? a.

Ensuring regular and adequate supply of funds to the organization b. Ensuring adequate returns to the shareholders c. Ensuring optimum utilization of funds d. Ensuring safety on investments made e. Ensuring prompt payment of taxes 2. Who is entrusted with the responsibility of allocating funds to State Governments? a. Niti Aayog b. Planning Commission c. Finance Commission d. Union budget e. Home Ministry

Block IV: Financial Management 30 3.

Which of the following is not an example of non-budgetary activities? a. Central assistance paid directly to government agencies under various schemes b. Expenditure by state departments/agencies from user charges collected c. Public Private Partnership (PPP) Project d. Expenditure for rural infrastructure e. Imputed subsidy cost of Government Loans 4. The process of estimating the availability of financial resources and allocating them to various activities based on a pre-determined priority is called a. Resource allocation b. Financial management c. Budgetary process d. Tax planning e. Non-budgetary activities 5. Which of the following is a prominent source of funds for the Government? a. Borrowings b. Ways and Means advances from RBI c Tax revenue d. Revenue from government undertakings e. Grants in aid Activity 10.1 1. Discuss the role of Niti Aayog. What do you think was the reason for replacing Planning Commission with Niti Aayog? 2. Go through the recent budget announced by the Finance Minister and list any 10 items of budget allocations.

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Funding in Government Agencies and Undertakings In case of Government agencies, the respective Ministries/Departments provide the estimates relating to each of the public enterprises (budgetary support, internal and extra budgetary resources and total plan outlay) before framing the Budget. Most of the Government Undertakings raise funds in the form of equity through public and internal accruals. In case of public sector banks, the funds are raised through Tier I and II capital. Navaratnas such as BHEL, ONGC, NTPC, etc., are profit-making units and raise the funds through normal sources such as bonds, Bank borrowings, equity from the public etc. In case of loss making units, based on the need, the government provides budgetary provisions. Government has also disinvested in some of the undertakings and the process is on. Exhibits 10.4, 10.5 and 10.6 provide the details of sources of funds for BHEL, a public sector Navratna company.

Exhibit 10.4: Sources of funds for BHEL as on 31-03-2021 Particulars ` in crores Share Capital 696.41 Total reserves 25,787.64 Total shareholders' funds 26,483 Long term borrowings 8,895.53 Total current liabilities 20321.66 Source:

[https://www.moneycontrol.com/india/stockpricequote/infrastructuregeneral/bharatheavylectricals/BHE](https://www.moneycontrol.com/india/stockpricequote/infrastructuregeneral/bharatheavyelectricals/BHE)

Exhibit 10.5: Audited balance sheet as on 31.3.2021 (` in Crores) Liabilities Amount Assets Amount Share Holders funds 26,484.05 Non-Current assets 28334.02 Non-Current Liabilities 8,895.53 Current assets 27367.22 Current Liabilities 20321.66 Total 55701.24 Total 55701.24 Source-

BHEL Annual Report, 2021 <https://www.bhel.com/sites/default/files/BHEL%20Annual%20Report%202020%2021%20Integrated.pdf>

Exhibit 10.6: Operating performance for the Year Ending March 31, 2020 and 2021 (` in Crores)

Particulars March 2021 March 2020 Total Revenue 17308.44 21459.19 Operating Profit (3982) (1243) Other income 369.84 580.58 Net Profit (2717.14) (1472.97) Source:

BHEL Annual Report, 2021 <https://www.bhel.com/sites/default/files/BHEL%20Annual%20Report%202020-2021%20Integrated.pdf>

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BHEL reported an operating loss and net loss in both the years 2020 and 2021. However, the company's current ratio is 1.35 indicating that the liquidity position is moderate though it is less than an ideal ratio of 2:1.

The leverage ratio, also at comfortable level of 0.33. 10.5 Funding Needs of Various Types of Entities In the previous sub-topic we have understood the need for finance for governments. Similar to this, individuals, business entities also require funds for conducting their activities. Such funds requirement is for a short term or a long term period. In other words, these people may require funds as a temporary finance for a short term or long term finance. 10.5.1 Overview of Short-term and Long-term Instruments Any Government/ business/ individual entity needs two types of funding - long- term funds and short-term funds. Long term funds are needed to set up the unit, diversification, expansion, modernization and similar capital expenditure investments. These investments need huge funds and are procured from long- term sources. Thus, long-term funds are needed to finance acquisition of fixed assets. Similarly, these entities also need short-term funds for its day-to-day operations, also called working capital funds.

The various sources of finance (long term and short term) are depicted in the following Figure 10.1: Figure 10.1: Sources of Finance for Various Entities Source: ICFAI Research Center 10.5.2

Government

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Securities A Government security is a tradable instrument issued by the Central Government or the State Governments.

Such securities, called treasury bills, are short term with

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mangal . Intoduction to Financial Markets & In ... (D22478819)

original maturities of less than one year. The long-term Government bonds or dated securities have original maturity of one year or more. In India, the Central Government issues both treasury bills and bonds or dated securities State Governments

also raise loans, from the market, called State Development Loans (SDL). SDLs are dated securities issued through an auction similar to the auctions conducted for dated securities issued by the Central Government. Interest is serviced at half-yearly intervals and the principal is repaid on the maturity date.

Sources of Finance Long Term Equity, Preference shares, internal accruals, Bonds, Term loans (Banks & NBFCs) and others Short Term Working capital from Banks, Commercial papers, Short term loans from NBFCs and others

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Dated Government securities are long-term securities with a tenor up to 30 years. They

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mangal . Intoduction to Financial Markets & In ... (D22478819)

carry a fixed or floating coupon (interest rate) paid on the face value and is

paid at fixed periods. These Government

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securities are issued through auctions conducted by the RBI on the electronic platform called the NDS.

The Public Debt Office (PDO) of the Reserve Bank

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of India acts as the registry / depository of Government securities and deals with the issue, interest payment and repayment of principal on maturity. Most of the dated securities are fixed coupon securities.

Treasury bills or T-bills are money market instruments and are short-term debt instruments issued by the Government of India and are presently issued in three tenors, namely, 91 day, 182 day and 364 day. Treasury bills are zero coupon securities and

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pay no interest. However, they are issued at a discount and redeemed at the face value at

83%**MATCHING BLOCK 23/173****SA**

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no interest. However, they are issued at a discount and redeemed at

the time of maturity. The Reserve Bank of India conducts auctions usually every Wednesday to issue T-bills. Payments for the T-bills purchased are made on the following Friday. The 91 day T-bills are auctioned on every Wednesday while 182

54%**MATCHING BLOCK 25/173****SA**

003_Banking and Indian financial _16-7-13.pdf (D142522847)

day and 364 day tenure T-bills are auctioned on alternate Wednesdays. The Reserve Bank releases an annual calendar of T-bill

issuances for a financial year in the last week of March of the previous financial year. The Reserve Bank of India announces the issue details of T-bills through a press release every week.

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FMG-302 Indian Financial System and Management ... (D164737022)

Government of India, in consultation with the Reserve Bank of India,

also issues a new short-term instrument, known as Cash Management Bills (CMBs),

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to meet the temporary mismatches in the cash flow of the Government.

The CMBs have the generic character of T-bills, but are issued for maturities less than 91 days.

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mangal . Intoduction to Financial Markets & In ... (D22478819)

Government of India also issues savings instruments (Savings Bonds, National Saving Certificates (NSCs), etc.) or special securities (oil bonds, Food Corporation of India bonds, fertilizer bonds, power bonds, etc.).

These are usually not tradable.

Government entities often approach the debt market to borrow as they consider this mode of raising funds to be comparatively inexpensive and with lesser restrictions when compared to bank financing. Exhibit 10.7 provides an example of this form of borrowing by Godrej Industries. Exhibit 10.7: Debenture Issue by Godrej Industries in September 2021

Godrej Industries carries a 125 year old legacy of its holding company, the Godrej Group, established in the year 1897. The company operates

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in consumer goods, real estate, agriculture, chemicals and financial services

industries 8 . On September 29, 2021, Godrej Industries decided to raise ₹ 750 crore through the issue of non-convertible debentures (NCDs). Contd.... 8

<https://www.godrejindustries.com/know-us/our-story/footer>

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The management committee of the company took the decision to issue 7,500 rated, listed, unsecured and redeemable NCDs having a face value of ₹ 10 lakh amounting to ₹ 750 crore. The company plans to take the place

placement route for issue of these NCDs, which will carry a tenure of 7 years. These NCDs come with a coupon rate of 7.58 percent per annum, payable annually.

The bond issue was rated as AAA by both CRISIL and ICRA.

Source-<https://economictimes.indiatimes.com/markets/companies/godrej-industries-raises-rs-750-cr-via-ncds/articleshow/86591887.cms>, Sept, 2021 10.5.3

Corporates Corporates similar to governments raise funds both long and short term for their capital and working capital needs. They, however raise the funds based on their individual financial strengths and past performance unlike the Governments who rely on their Budgetary estimates and grants. The finance Manager plays an important role in resource mobilization based on the future estimates, which are worked out on the past performance and market demand for the products. Short-Term Resources The most important sources of short-term funds for companies are through working capital facilities from the banks. These facilities are assessed by the Banks based on the CMA data provided by the company and the liquidity position based on the latest financial statement. The pre sales finance (cash credits), post sales finance (Bills), Letters of credit (Foreign and Inland), short- term facilities, etc. are a few of them. Another important source of short term funds for corporate are

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Commercial papers (CP) -an unsecured money market instrument issued in the form of a promissory note.

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Commercial papers (CP) -an unsecured money market instrument issued in the form of a promissory note. It			
91%	MATCHING BLOCK 33/173	SA	023E2430_Financial Markets and Institutions.pdf (D165201762)
an unsecured money market instrument issued in the form of a promissory note. It was introduced in India			
88%	MATCHING BLOCK 32/173	W	
introduced in India in 1990 with a view to enable highly rated corporate borrowers to diversify their sources of short-term borrowings.			
100%	MATCHING BLOCK 34/173	SA	Shivani Sharma, final thesis.pdf (D30330450)
enable highly rated corporate borrowers to diversify their sources of short-term borrowings.			

Normally the

cost of funds mobilized through this way is less compared to Banks. Long-Term Sources As in case of short-term finance, banks are the major source for long-term finance for investment in capital assets. The other long term sources available to the companies are through equity (IPO and subsequent public offers), internal accruals, leasing, Bonds, deferred payment options offered by the manufacturer, etc. In case of term loans from banks, the company has to provide 25% margin on the value of assets to be procured through either internal accruals or additional equity and the assessment of the credit limit by the banks be based on the capital gearing ratio of the company. Corporate bonds are transferable secured and unsecured debt instruments issued by corporate to a broad base of investors. Secured bonds are backed by a specific pledged asset or other form of collateral. If the issuer defaults,

Unit 10: Financial Management Process 35

bondholders have the right to liquidate its assets and recoup as much of their investment. In case of unsecured bonds, known as debentures, the debt is backed solely by the credit worthiness of the borrower. The participants comprise the market players – investors on the demand side and issuers on the supply side. Guaranteed bonds 9 , Zero coupon bonds 10 , Income bonds 11 , Euro bonds, Euro dollar bonds 12 , Masala bonds (refer to Exhibit 10.8),

Maharaja Bonds 13 are a few of them. 10.5.4

Individuals Individuals unlike corporates and Government raise funds only from banks and financial institutions (NBFC/ DFI) through short, medium and long term for various needs. Long-term loans over 10 to 30 years are mostly in the form of housing loans for purchasing house property. Medium term loan is for acquiring capital goods like furniture, electronic goods, 2 and 4 wheelers repayable in 2 to 7 years. Personal loans and clean loans for short-term needs are normally repayable within 2 years. The salary drawn by the individual is considered to assess the loan component by the lending institution and these are classified as retail loans.

10.6 Corporate Financial Management Though financial management as a discipline is essential to everyone, be it an individual, a business entity or government, the subject has wider applications in the corporate world. This sub section deals with financial management in the context of a corporate entity. 10.6.1 Interface of Finance with Other Functions You will recall that in our introductory chapter we described the pervasive nature of finance. Let us discuss in detail the reasons why knowledge of the financial implications of the finance manager's decisions is important to the non-finance managers. One common factor among all managers is that they use resources and since resources are obtained in exchange for money, they are in effect making the investment decision; and in the process of ensuring that the investment is effectively utilized, they are also performing the control function. Marketing-Finance Interface The Marketing Manager takes many decisions, which have a significant impact on the profitability of the firm. For example, he should have a clear understanding of the impact of the credit extended to the customers on the 9

Guaranteed bonds – the interest and principal repayment is guaranteed by third party 10 Zero coupon bonds – No interest is paid; it is traded at a discount 11 Income bonds – there is no guarantee of payment of interest 12 Euro bonds and Euro dollar bonds – Euro bonds are denominated in any other currency other than the home currency while Euro dollar bonds are US – Dollar denominated bonds 13 Maharaja Bonds – Rupee denominated bonds

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profits of the company. Otherwise, in his eagerness to meet the sales targets he is likely to extend liberal terms of credit, which may put the profit plans out of gear. Similarly, he should weigh the benefits of keeping a large inventory of finished goods in anticipation of sales against the costs of maintaining that inventory. Other key decisions of the Marketing Manager, which have financial implications, are pricing, product promotion and advertisement, choice of product mix and distribution policy. Production-Finance Interface In any manufacturing firm, the Production Manager controls a major part of the investment in the form of equipment, materials and men. He should so organize his department that the equipment under his control is used most productively, the inventory of work-in-process or unfinished goods and stores and spares is optimized and the idle time and work stoppages are minimized. If the production manager can achieve this, he would be holding the cost of the output under control and thereby help in maximizing profits. He has to appreciate the fact that while the price at which the output can be sold is largely determined by factors external to the firm like competition, government regulations, etc. the cost of production is more amenable to his control. Similarly, he would have to make decisions regarding make or buy, buy or lease, etc. for which he has to evaluate the financial implications before arriving at a decision. Top Management-Finance Interface The top management, which is interested in ensuring that the firm's long-term goals are met, finds it convenient to use the financial statements as a means for keeping itself informed of the overall effectiveness of the organization. We have so far briefly reviewed the interface of finance with the non-finance functional disciplines like production, marketing, etc. Besides these, the finance function also has a strong linkage with the functions of the top management. Strategic planning and management control are two important functions of the top management. Finance function provides the basic inputs needed to undertake these activities. In view of the recent liberalization of the Indian economy, abolition of the office of the Controller of Capital Issues (

who used to fix issue prices beforehand) and efforts of the Indian economy towards globalization, finance managers are exposed to some new challenges. 10.6.2

Sources and Uses of Funds of Corporates Funds flow analysis is an important analytical tool for developing information to be used in financial decision making. It

is a statement that explains the various sources from which funds are raised and used in various Assets. This statement captures the flow of funds and is useful to understand how the business financed its assets, how the inventory is built up, how the liabilities

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have been discharged, dividends and taxes paid, etc. It also gives us an idea as to how the business has managed to meet the capital and revenue expenditure etc. The funds flow statement is prepared for a specific period by finding out the difference between the corresponding balance sheet items at the beginning and end of the period. All increase in liabilities and decrease in assets are sources of funds and all the decrease in liabilities and increase in assets are application of funds.

The typical funds flow statement based on total resources is shown as hereunder. Sources of funds Application of funds 1. From operations a. Profit after tax b. Depreciation and other non-cash charges 2. Issue of equity 3. Increase in liabilities 4. Decrease in assets 1. Dividends 2. Decrease in liabilities 3. Increase in assets Example - Consolidated Cash flow as on 31.03.2021 of BHEL

Particulars (₹ in crores) Net cash flow from operational activities 561.72 Net Cash

used in investment activities (42.55) Net Cash used in

financial activities (394.85) Net increase in cash 124.32

Importance of funds flow statement Funds flow statement helps the analyst to gain various insights into the operation of the company. It helps us in the detection of imbalances and taking necessary corrective measures. It helps us to appraise the performance of the various divisions of the company if it has any. It also provides us with information about the portion of the company's growth that is funded by internal accruals and that which is funded externally. Funds flow analysis also helps to plan the future requirement of funds. Income from Operations This is one of the main sources of funds for a company. Income from operations is the profit generated by the operations of a business. This classification of income excludes gains and losses from the sale of assets, interest income, interest expense, and any other income not related to the core operations of the firm. It is the ability of a company to earn money on an ongoing basis and a true measure of the company's efficiency.

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For example, from operations, BHEL has achieved net revenue of ₹ 17308.44 crores for the year 2020-21 as against ₹ 21459.19 crores in 2019-20. The

company reported an operating loss of ₹ 3982 crores in 2020-21

The operating profit margin is one of the important profitability ratios that measures what percentage of total revenues is made up by operating income. In other words, the operating margin ratio shows the amount of revenues that remain after all the variables or operating costs are paid. This ratio is a key indicator for investors and creditors to see how businesses are supporting their operations. If companies can make enough money from their operations to support the business, the company is usually considered more stable. On the other hand, if a company requires both operating and non-operating income to cover the operation expenses, it shows that the business's operating activities are not sustainable.

Investments in fixed assets

Investments in fixed and current assets form an important part of application of funds. Investments in fixed assets are strategic investments. These investments have long term effects and are irreversible as they involve substantial outlays. Investment in fixed assets involves thorough planning, analysis, selection, funding, implementation and timely review, which normally form the various stages of capital budgeting itself. One of the important aspects of investment in fixed assets after a proper analysis is the funding pattern and the assessment of cost of capital. The projected profitability and the debt servicing capacity of the company form the yardstick in determining the investment in fixed assets. Breakeven point and debt service coverage ratios are important tools to determine while funding the project. The major components of investment in fixed assets are land, building, plant and machineries, and other fixed assets. Increase in fixed assets leads to application and decrease in fixed assets (other than depreciation) leads to source of funds.

Investments in Current assets

This investment is basically in working capital and is tactical unlike strategic in case of investing in fixed assets. It is also working capital management, which not only involves investment in current assets, but also managing current liabilities as they form the other source of financing such as sundry creditors and letter of credit arrangement. The components of current assets include inventory (Raw material, Semi finished goods and finished goods), Receivables, Cash and Bank balance, Prepaid expenses and other advances. The required working capital of a company is financed by banks, creditors and funds raised through commercial papers. The pre sales facility sanctioned by the bank is cash credit / overdraft facility and post sales through bills financing / discounting.

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A borrower can draw as often as he requires provided the outstanding does not exceed the cash credit / overdraft / bills limit. As regards the funds flow from working capital, any increase in current assets or decrease in liabilities increases the capital while any decrease in current assets or increase in current liabilities results in decrease of working capital. Distribution of income as dividends

Dividend is the return a shareholder gets for the risk taken by him in investing in a company in the form of equity. This is the payment made by a company by distribution of a share in profits while the remaining quantum of profits or surplus is re-invested in the business. Dividend to shareholders is usually deposited into the bank account of the investor. Sometimes the corporation has a dividend reinvestment plan and this amount can be paid by the issue of further shares or share repurchase. The shareholder gets the dividend in proportion to his share holding and it is normally a fixed amount per share. Distribution of dividend is the application/ use of funds as it involves funds outflow. Various ways of procuring funds Funds procured for a project are a source of income. Funds procured can be broadly classified into two types: equity and debt. Equity ? This can be raised both through private and public sources. Capital raised through public sources is traded through stock exchanges. Private sources include equity, preference shares, debentures which are placed with a small group of investors like private equity funds, financial institutions etc. Preference capital – This is a form of hybrid financing with some of the characteristics of equity and some of debentures. The investors will get preference dividend from the profits generated by the company. It also resembles debentures as the dividend is fixed. The claim on dividend by preference shareholders is prior to the claim by equity holders. However, the preference shareholders do not have a right to vote. There are various types of preference shares - Cumulative and Non-cumulative, convertible and non-convertible, redeemable and non-redeemable etc. Internal accruals – This source combines the depreciation charges and retained earnings. Retained earnings are that portion of the equity earnings (PAT less preference dividends) which are ploughed back in the firm. Bonds / debentures - Bonds/ debentures are another important source of funds for a company and an alternative to term loans from banks and financial institutions. The obligation of a company to a bond/ debenture holder is similar to a borrower who takes loans from banks. The company has to service interest regularly and the principle on the date of maturity.

Block IV: Financial Management 40 There are various types of bonds such as deep discount bond, floating rate bonds, indexed bonds, convertible debentures, etc. Any increase in bonds and debentures is a source and decrease is application of funds.

Commercial Paper - This is a short term unsecured promissory note issued by highly rated corporates with a maturity period up to 180 days. The CP is sold at a discount and redeemed at face value

by the investor. CPs are directly placed with a few investors. It is also, another way of procuring working capital funds. Normally, the cash credit funds are earmarked by the bank to the extent of CPs issued. The CP market is not so well developed in our country.

Term Loans - Term loans are the primary source of long term funds to individuals and corporates, historically, to acquire fixed assets. Term loans are secured advances by banks and other financial institutions and are self- liquidating in nature over the repayment period unlike working capital. Capital gearing and debt serving capacity are the main aspects looked into while considering the term loan limit by the funding institution. Increase in term loans indicates flow of funds and reduction is application/ uses of funds.

Working Capital - Working capital facilities are the most important short term source of funds to corporate for operational requirement and mainly for acquiring current assets such as inventories and post sales finance such as bills. There are three ways of financing this facility by banks - Overdrafts / cash credits, Letter of credit and purchase or discount of Bills. Liquidity ratios are an important type of working capital facility by banks. In funds flow analysis, any increase in working capital funds is a source and reduction is application of funds by the corporate. Other types of funds - Apart from the sources mentioned above, there are a few more such as: a. Deferred credit (Sellers credit) b. Lease and hire purchase finance c. Unsecured loans and deposits d. Short term loans e. Factoring f. Securitization

Forms of Investment Instruments Investment instruments are financial claims by the investor in a company or government security. The price of these instruments is determined by the market. The investment instruments can be broadly classified as follows.

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Figure 10.2: Classification of Investment Instruments Source: ICFAI Research Center

Government securities are treasury bills, bonds, dated securities etc. Private securities are shares, debentures, bonds, CP, derivatives such as option swaps, futures, forwards, Certificates of deposit, deposit receipts etc. Most of these securities are in demat form now. While the long term securities comprise of shares, debentures etc., the short term market referred to as money market consists of treasury bills, certificate of deposits, commercial paper etc.

10.7 Financial Management for Individuals Financial management for an individual or a family is called personal financial planning. Its importance is very much relevant now in view of globalized economy and increasing dynamic situation. For example, demonetization of currencies (₹ 1000 & ₹ 500) has created a new situation where the banks have reduced the interest rates drastically by almost 100 basis points in November – December 2016 and thereby reduced the income to the individual investors. The quality of life we lead has undergone radical changes in the past decade and people like to lead a comfortable life with luxury, which is possible if we can have a well-thought-out financial plan. One of the major benefits of financial planning is that it helps us to acquire, use, control and manage our financial resources most effectively. A good financial plan can help us to define our short and long term goals, develop appropriate financial program to achieve them in an effective and efficient way and help to maintain the quality of life. The basic steps in building a comprehensive financial plan are: a. Assess the financial position b. Define the goals (Short and long term) clearly c. Develop an appropriate plan to achieve the goals d. Implement the time bound plan e. Evaluation at regular intervals and make mid-course correction if necessary. f. Review the plan.

Forms of Investment Instruments Nature Government & Private Term Long term and Short term (Capital and Money market)

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Individual's sources of income and expenditure An income and expenditure statement of an individual provides the details of income from various sources, expenditure incurred and the surplus generated. The income component comprises all the cash in-flows, which include salaries, wages, loyalty, honorarium, commissions, interest/ dividends earned on investments, rent received from house property etc. The income statement should also reflect the capital gains made by sale of investments in a particular year. The expenditure statement is of the cash out-flows and should show all the expenditure and purchases made in the year. This includes food, clothing, transport, rent paid, medicines, repairs, utility services like electricity, water, gas, petrol, etc., insurance premium, municipality taxes, credit card payments, etc. It also records all the purchases made which may include electronic goods, vehicles etc. It also covers the interest and principle amount paid on the loans taken from banks and other financial institutions. The first stage of preparation of this statement is to list out all the income and receipts on one side and all expenses and purchases on another side. To make it more professional, the second step is to classify the income and expenditure into various heads as shown in Table 10.1:

Income	Expenditure
Wages	Salaries
Housing	Professional Fees
Utilities	Honorarium
Received	Food
Bonus & Commission	Transport
Income from Investments	Medical Expenses
Others	Clothes
Insurance	Taxes
Purchases	Miscellaneous
Cash Surplus	Total Income
Total Expenditure	

Source: ICFAI Research Center 10.7.2

Where to Invest? (Investment decision) The money that is earned has to be properly put to use. A part has to go for expenses and a part towards savings. Investment refers to the money saved and invested in various instruments. It can be both in short term and long term. The main points that one has to ponder before taking an investment decision are: 1. What are my objectives for investing in a particular instrument? 2. Where should I invest? It is advisable to start investing at an earlier age to get the benefits of compounding.

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Some of the important objectives of investments are: a. Earn returns which can support source of funds b. Purchase assets which can improve the standard of living c. To achieve the financial goals such as purchasing a house, supporting children's education, marriage. d. Save for future requirement (post retirement) to maintain the same standard of living. Investment decision by an individual depends on his risk taking capability and appetite. There are various options available now for investments based on the risk appetite of the investor and can be broadly classified into Financial Institutions (Banks, NBFC, Mutual funds, Insurance, etc.) and Financial markets (capital markets, money markets and derivative markets such as options, futures, etc.). Insurance plays a significant role in creating and protecting our wealth. Individuals are exposed to various types of risks such as death, ill-health, credit, loss due to damage of property, vehicle theft or accident etc. One should evaluate these factors and take suitable cover to protect his wealth and health. Premium paid towards the insurance policy is eligible for deductions and thereby reducing taxable income. Investing in certain instruments and assets will minimize the taxable income and is a part of tax planning. One such opportunity for investors is taking a housing loan and investing in flats / homes. Interest and principle repayment will qualify for tax benefits.

10.7.3 How to Procure Funds? (Financing decision) The major source of funds for individuals for investments is from the savings, followed by loans from banks. Long-term investments need long-term source and short-term investment needs short-term financing source. Savings is long-term source of funds and so are housing loans, vehicle loans etc. These funds can be invested in long-term assets such as investing in house, equities, mutual funds, etc. where the lock-in period normally is over 3 to 5 years. Credit card loans, personal and clean loans are normally short-term in nature and can be used for acquisition of short-term assets or personal expenditure. It is essential to keep in mind one's savings and repayment capacity in short-term period before embarking on taking such loans. For example, one should not venture into taking a loan of higher amount and longer repayment when his salary and other income cannot support the matching EMI payments.

10.7.4 Goals of Personal Financial Management Every person has a goal of financial management and this goal differs from person to person. However, there are some common basic goals of financial management, which everyone should achieve in life, like wealth maximization.

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The personal financial goals have to be classified into short term, Medium term and long term goals and necessary funds have to be allocated for achieving these goals. For an individual the goals can be listed as follows. a. To meet monthly expenses for self and family and save 25 to 30 % of earnings for future needs (Short Term) b. To meet other expenses like repairs , purchase of mobiles, laptops, etc. (Short Term) c. To provide funds to meet unexpected expenditure. (Short Term) d. To plan for purchase of house/ car, etc., and to lead a decent life.(Long Term) e. To get the children's education (Long Term) f. To provide funds towards retirement (Retirement plan) (Long Term) A comprehensive financial plan will enable an individual to achieve wealth maximization, meet financial needs and achieve other financial goals.

10.8

Environment of Finance One of the important aspects of a Finance Manager's job is to understand the external environment in which he operates. In a country like ours where investment and financing activities are subject to numerous governmental controls and legislations, a finance manager must have a thorough understanding of the legal framework circumscribing his decisions. Let us consider the following examples to clarify the point: ?

With the Make in India initiative announced by the Central Government in 2014, a number of project announcements came from the corporate sector. For instance, Spice Group announced a ` 500 crore investment in setting up a manufacturing unit in Uttar Pradesh. ?

Wal-Mart Stores Inc (Wal-Mart), the world's largest retailer, and Bharti Enterprises Ltd. (Bharti), a leading business group in India established a joint venture to enter into

the

Indian retail industry. Though the venture made an initial investment of USD 100 million, which would further increase to USD1.46 billion, it has restricted its business to only the cash- and-carry segment of Indian retail industry. Here foreign retailers of multi-brands were only permitted to operate through franchises and licenses, or a cash-and-carry wholesale model in India; therefore, the financial manager cannot recommend more investment in one segment of the industry.

The examples above clearly drive the point that the regulatory framework has a significant influence on the investment and financing decisions of a business. However, a related question that arises is whether there are any other external factors besides legal provisions and governmental regulations that also intervene in the decision-making process of the finance manager. The answer

to this question is in affirmative. The form of organization that a business entity adopts

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often limits the investment and financing options. For instance, a partnership firm engaged in trading yarn cannot follow Reliance Industries Limited to

set up a ` 400 crore petrochemical complex because the partnership form of organization limits both the size and the ability to mobilize such massive funds. Additionally, the structure of the financial markets from where the finance manager has to raise funds and the regulations governing the financial intermediaries (like banks and financial institutions) impact the decisions of a finance manager.

In addition, the finance manager cannot ignore the tax factor. Therefore, when he is evaluating the feasibility of the investments, the finance manager should also consider the fiscal (tax) factors associated with these investments. Therefore, we find that the Finance Manager pursues his objective of owners' value maximization within a set of external constraints besides the internal constraints that crop up from the inherent strengths and weaknesses of each entity. This makes his job complex and interesting because he has to make optimal decisions within the framework of these constraints. This sub section

seeks to create an awareness and appreciation of the intervening environmental variables.

From the above discussion, we can zero in on four factors from

the external environment that directly influence the work of the Finance Manager. They are: ? Forms of Business Organization. ?

Regulatory Framework. ? Financial System (which will include financial markets and intermediaries). ? Tax Aspects. 10.8.1 The

Important Forms of Business Organization Sole Proprietorship This form of business organization is owned

and managed by a single person. The proprietor/owner is responsible for taking and assuming all the risks for his/her concern.

Hence, he also enjoys all the rewards, profits of the enterprise, bears all the

losses and incurs all the liabilities of the business. The merits of a sole proprietorship business are: ? Easy and inexpensive to set up. ?

Limited number of governmental regulations. ? Absence of firm tax. The demerits are: ?

Life of the firm is limited to the life of the owner. ?

Unlimited personal liabilities. ? Outside fund raising is not possible and can result in lack of growth. ? Tax on the income will be very high.

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Partnership In this type of firm, the

business is owned by two or more persons. They are partners in business and they bear the risks and reap the rewards of the business. The partnership comes into being through a partnership agreement or a partnership deed. Partnerships are governed by Indian Partnerships Act, 1932. The merits of the partnership firm are: ? Simple, like a sole proprietorship organization, it can also be set up easily and is less expensive. ? It is relatively free from governmental regulations. ? The expertise and experience of the partners are useful to the firm's operations. The demerits are: ? The existence of the firm depends upon the agreement between the partners. If any of them withdraws, dies or becomes insolvent, it may result in dissolution of the firm. ? The firm's existence is exposed to any conflicts between the partners. ? The partners have unlimited liability, so even their personal assets may be exposed to firm's decisions. To overcome this disadvantage the new Company law provides setting up Limited Liability Partnership ? Since the number of partners is limited, the firm's ability to raise funds is also limited. Companies A company is a voluntary association of persons formed for the purpose of doing business, having a distinct name and limited liability. It is a juristic person having a separate legal entity distinct from the members who constitute it, capable of rights and duties of its own and endowed with the potential of perpetual succession. Companies are those business entities that are incorporated under separate enactments. They have a distinct legal personality, separate from the persons constituting it. The word 'corporation' or the word 'body corporate' is defined in Clause (11) of Section 2 of the Companies Act, 2013: "Body corporate" or "Corporation" includes a company incorporated outside India but does not include – ? A co-operative society registered under any law relating to co-operative societies; and ? Any other body corporate not being a company which

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the Central Government may, by notification in the Official Gazette, specify in

this behalf.

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A company under the Company Law is a company incorporated under this Act or under any previous company law [Section 2(20)]. A company is allowed to incorporate only for a lawful purpose. A company can be either a public company, private company or a one-person company. One person company is a form of private company. To form a company, a requisite number of persons decide the type of company to be incorporated. To incorporate a public company, seven or more persons are a requisite number. For a private company, two or more persons and for one- person company, one person is the requisite number. The said persons shall subscribe their names or name to a memorandum of the company and fulfill all the requirements of incorporation stated in the Companies Act, 2013. [Section 3(1)]

A group of persons working together towards a common objective is a company. It represents different kinds of associations, be it business or non- business.

Private Company As per Section 2(68)

of

the Companies Act 2013, a private company means a company which has a minimum paid-up capital of one lakh rupees or such higher paid-up capital as may be prescribed and by its articles,

a. Restricts the right to transfer its shares, b. Limits the number of its members to two hundred not including i. Persons who are in the employment of the company; and ii. Persons, who having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased; c.

Prohibits any invitation to the public to subscribe for any securities of the company; moreover, where two or more persons hold one or more shares in a company jointly, they shall be treated, for the purposes of this definition, as a single member. Here are some of the important aspects to know about a private company: a. There is Restriction on Transfer of Shares b. There is Limitation on the Number of Members c. Cannot issue Prospectus inviting the public to subscribe for securities of the company. Privileges Enjoyed by Private Companies: As there are restrictions on raising money and maximum number of members in a private company, there is not much public accountability. Therefore, a private company need not be subjected to such a rigorous surveillance as in the case of

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a public company. The exemptions enjoyed by a private company are mentioned below. Exemptions i. A private company need not have more than two directors as against minimum three in the case of a public company. In case prescribed, one among the two shall be a woman director (Section 149). ii. The directors of a private company are not required to retire by rotation unlike in a public company where 2/3rds of the directors must retire by rotation at each annual general meeting (Section 152). iii. Quorum required for the general meeting in the case of private company is two persons as against five persons in the case of public company (Section 103). iv. A private company, by virtue of restriction on the public participation, is exempt from all the requirements of the Act relating to the prospectus (Section 103). One Person Company One Person Company (OPC) is the company introduced for the first time in the Companies Act, 2013. This is in addition to a private company and a public company under this Act. An OPC means a company having only one person as its member. [

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Section 2(62) of the Companies Act, 2013] Public Company According to Section, 2(71) of The Companies Act, 2013,

a 'public company' means a company which, a.

Is not a private

company. b. Has a minimum paid-up capital of five lakh rupees or such higher paid-up capital, as may be prescribed. c. Is a private company, which is a subsidiary of a company, which is not a private company. However, a company registered under Section 8 of the Companies Act, 2013

shall not be required to have the minimum paid-up capital for its incorporation. The Act is silent on this. 10.9 Regulatory Framework Our objective in this unit will be to highlight the salient features of the regulatory framework.

Corporate investment and financing decisions are circumscribed by a governmental regulatory framework, which seeks to (a) define avenues of investment available to business enterprises in different categories, ownership- wise and size-wise; (b) induce investments along certain lines by providing incentives, concessions, and reliefs; and (c) specify the procedure for raising

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funds from the financial markets.

The important elements of this framework are: (i) Industrial Policy, (ii) Industrial Licensing Provisions and Procedures, (iii) Regulation of Foreign Collaborations and Investments, (iv) Foreign Exchange Management Act, (v) Competition Act, 2002, (vi) Companies Act, 2013 and (vii) SEBI. In this section, we will discuss the salient features of these legislations/regulations and their implications for financial management.

Industrial Policy A finance manager of an enterprise must be aware of the provisions of the Industrial Policy Resolutions, 1956, Industrial Licensing Policy, 1973, and the Industrial Policy Statements made by the government from time to time because these provisions define the investment avenues open to an enterprise. In recent years, the government has initiated the process of liberalizing its policy towards participation of large industrial enterprises in different industries and streamlining the licensing procedures to expedite industrial development. The important policy measures announced in the recent past include: ? Abolition of licensing requirements except in the case of a selected list of eight industry groups. ? Raising the investment ceilings for small-scale industries and ancillary units. ? Removal of Monopolies and Restrictive Trade Practices (MRTP) limits on assets for companies. ? Permitting the private sector to enter the telecommunication equipment manufacturing industry. ? Encouragement for foreign investment up to 51% equity of a company. On a select basis, foreign investment in 100% subsidiaries is also being encouraged nowadays. ? Disinvestment in selected public sector units. **Industrial Licensing Provisions and Procedures** To regulate and develop industry in accordance with the objectives of the Industrial Policy Resolution and the priorities under the Five-Year-Plans, the government introduced the system of Industrial Licensing. To provide a legal framework for the system of licensing, the government enacted the Industries (Development and Regulation) Act, 1951. The existing system and procedures for industrial licensing have undergone a drastic change pursuant to the statement on Industrial Policy, tabled in both the Houses of Parliament on July 24, 1991. The statement has substantially reduced the requirement for various types of industrial approvals. Consequently, to implement this policy statement in respect of industrial licensing, a notification has been issued under the Industries (Development and Regulation) Act, 1951.

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The notification has three schedules: Schedule I: Lists the industries reserved for the

public sector. Industries included in this schedule are Mineral Oils, Mining, Railways, Defense-related industries and Atomic Energy. Schedule II: Lists the industries, which are subject to compulsory Licensing. It includes industries like Coal & Lignite, Petroleum, Sugar, Asbestos, Raw hides, Patent Leather, Tobacco, Motor cars, Paper and Newsprint, Industrial explosives, Hazardous chemicals, Drugs and Pharmaceuticals and Entertainment electronics. Schedule III: Lists the articles reserved for the small-scale/ancillary sector, which include Textile products, Food & Allied industries, Wood, Paper products, Leather products including Footwear, Rubber, Plastic products, Chemicals, Dyes, Tiles, Glass and Ceramics. The provisions of the revised industrial licensing policy are as follows: ? Industrial licensing is abolished for all projects except for a short list of industries (Schedule II) related to security and strategic concerns, social reasons, hazardous chemicals and overriding environmental reasons, and items of elitist consumption. Industries in the small-scale and ancillary sector are exempted from licensing all articles of manufacture, which are not covered by Schedules I and II. ? Industries, where security and strategic concerns predominate, will continue to be reserved for the public sector (Schedule I). ? For projects requiring imported capital goods, automatic clearance will be given where foreign exchange availability is ensured through a foreign equity. Regulation of Foreign Collaborations and Investments Foreign collaboration involves either transfer of foreign technology (Technical collaboration) or transfer of foreign technology-cum-capital (Technical-cum- Financial collaboration). Technical collaboration entails outflow of foreign exchange in the form of royalty payments, while financial collaboration results in an outgo of foreign exchange in the form of dividend remittances and capital repatriation. Therefore, the government follows a selective policy in approving foreign collaboration projects. Even where it approves the collaboration in principle, it regulates the extent of foreign investment in the project, amount of royalty payments, and the terms and conditions of the collaboration agreement. Foreign Exchange Management Act The Foreign Exchange Regulation Act, 1973, regulated foreign investment in India. The Foreign Exchange Management Act (FEMA) replaced the Foreign Exchange Regulation Act (FERA) with effect from June 1, 2000.

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objectives of FEMA are: (i) to facilitate external trade and payments, and (ii) to promote an orderly maintenance of

the foreign exchange market in India. The Salient Features of the Act are: ?

Full freedom to a person resident in India who was earlier outside India, to hold or transfer any foreign security or immovable property situated outside India and acquired when he/she was resident there.

Similar freedom is also given to a resident who inherits such security or immovable property from a person resident outside India. ?

A person resident outside India is also permitted to hold shares, securities and properties acquired by him while he/she was resident in India. Similarly,

a person resident outside India is also permitted to hold

such properties inherited from a person resident in India. ? Exchange drawn can also be used for the purpose other than for which it is drawn provided the withdrawal

is otherwise permitted for such purpose. ? Any person can deal, transfer or pay pursuant to any foreign transaction only in accordance with the provisions of this Act or with general or special permission of the RBI to promote and for orderly maintenance of the foreign exchange market in India. ? The responsibility lies with such person resident in India to take all reasonable steps for realization and repatriation to India as prescribed by the RBI the amount of foreign exchange which is due or accrued to him unless otherwise provided in the Act. ? Every exporter of goods shall furnish to the RBI or to such authority a declaration as prescribed for the purpose of ensuring the realization of export proceeds by such exporter. The Competition Act, 2002 The object of the

Competition Act, 2002 is to position the competition policy with pragmatic options, to promote the spirit of competition and harmonize the conflicts caused by the volatility of globalized markets. The Act provides for a regulatory framework of rules covering the critical areas of competition namely: ? Anti-competitive agreements among enterprises. ? Abuse of dominant position in the market. ? Combinations/Mergers between enterprises.

The

Competition Act, 2002 aims at promoting free and fair competition in India, and protects the interests of consumers. The act provides for the

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establishment of a regulatory body called "Competition Commission of India" with the following basic functions: ? Administration and enforcement of law. ? Competition advocacy.

The

Competition Act, 2002 is a comprehensive enactment addressing contemporary concerns of competition and future possibilities that impact the sustainable economic development. The Act consists

of 66

Sections dealt under nine chapters covering the following areas: ? Prohibition of anti-competitive agreements. ? Prohibition of abuse of dominant position. ? Regulation of combinations. ? Establishment of Competition Commission of India. ? Penalties for contravention of orders of Commission and non-compliance with directions. ? Competition advocacy. ? Constitution of competition fund.

Figures 10.3 and 10.4 contain the provisions of Competition Act 2002 pertaining to anti-competitive agreements and activities that constitute abuse of dominant position. Figure 10.3: Classification of Anti-Competitive Agreements

Anti-competitive Agreements Vertical Agreements Horizontal Agreements (in relevant markets)

Tie-in Arrangements (Section 3.4(a)) Exclusive supply agreements (Section 3.4(b)) Exclusive distribution agreements (Section 3.4(c))

Resale maintenance (Section 3.4(d)) Prices Quantities Bids Market sharing Refusal to deal (Sections 3 and 4) Source: Competition Act, 2002

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Figure 10.4: Abuse of Dominant Position

Abuse of Dominant Position Exploitation of Market Protection of Dominance (through restrictive practices) Unfair discrimination in purchase/sale Predatory pricing (Sections 4.2ai x 4.2aii) Limiting production of goods/services (Section 4.26(ii)) Restricting technical/scientific development to the detriment of consumer. (Section 4.2b(ii)) Denial of market access (Section 4.2(c)) Tie-in arrangements (Section 4.2(d)) Migration (Section 4.2(e))

Source: Competition Act, 2002

Apart from dealing with the competition misconduct, the Act also envisages a promotional role. The Competition Commission of India has advocacy role in advising Government and creating awareness and imparting training on competition issues. The Act provides exhaustive coverage of business entities under definition "enterprise" (Section 2ch) by including: ? Industrial activities. ? Marketing activities. ? Services, including financial investments. ? Stock broking. Significantly, the Act also covers government departments engaged in "enterprise" activities excluding only sensitive wings like atomic energy, currency, defense and space. Companies Act, 2013 The major objectives of the Companies Act, 2013 are: ? To ensure a minimum standard of business integrity and conduct in the promotion and management of companies; ? To elicit full and fair disclosure of all reasonable information relating to the affairs of the company; ? To promote effective participation and control by shareholders and protect their legitimate interests; ? To enforce proper performance of duties by the company management; and ? To investigate into and intervene in the affairs of companies which are managed in a manner prejudicial to the interests of the shareholders or the public at large.

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The Companies Act, which has 657 sections attached with 15 schedules, is a very comprehensive legislation governing the functioning of companies. Many of the provisions of this Act have a direct bearing on the financial management of companies. The Act provides for matters like types of share capital that can be issued, issue of share capital, issue of debentures, loans, investments, inter-corporate investments, distribution of dividends, reorganization, amalgamation, and liquidation. Some of the important provisions of this Act related to the financial management of companies are listed below: ? A public limited company can issue only two kinds of shares – preference shares and equity shares.

A company as per section 53 of the Act cannot issue shares at a discount. Only redeemable preference shares can be issued which can be redeemed within 20 years of issue. ?

Any further issue of shares has to be first offered to the existing equity shareholders in proportion to the shares held by them, unless they waive this right. ? A company that completed a buy-back of shares or other specified securities under this section, shall not make any further issue of such shares or securities

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within a period of six months from the date of

completion of such buy-back subject to certain exceptions. ? Sweat equity shares are issued by the company as per section 54 to employees or directors at a

discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value

additions by whatever name called through a special resolution passed by the shareholders of such company in their general meetings, provided one year has elapsed from the date on which the company is entitled to commence business. ? No company shall make inter-corporate loans and investments exceeding sixty percent (60%) of its paid-up share capital and free reserves, or one hundred percent (100%) of its free reserves, whichever is more, unless it is approved by the shareholders of the company through passing a special resolution in their general meeting of the company, otherwise a Board resolution is sufficient. ? Dividends can be declared only out of the profits of the company arrived at after providing for depreciation in accordance with the provisions of Sec.123 or out of the profits of the company for any previous financial year or years arrived at after providing for depreciation in accordance with those provisions and remaining undistributed or out of both or out of moneys provided by the central government or state government for the payment of dividend in pursuance of a guarantee given by that government.

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The other provisions of the Companies Act, which can be of interest to us are the provisions related to the maintenance of accounts, their audit and disclosure to shareholders. The Act requires all companies to prepare the annual financial statements (Statement of

Profit & Loss and Balance Sheet) in the prescribed manner and format and get them audited by a Chartered Accountant. Further, a public company is required to present its audited financial statements to the shareholders for approval. These financial statements together with the Directors' Report, Auditors' Report and annexures to the financial statements as prescribed by the Act constitute the annual report of the company. Annual reports of companies are available to the public for inspection at the office of the Registrar of Companies in each State.

Tax Aspects A company incorporated in India or having its entire management and control in India is considered a resident company and is taxed under the provisions of the

Indian Income Tax Act, 1961 on its worldwide income. A non-resident corporation (foreign company) is taxed only on income derived in India from Indian operations, income that is deemed to arise in India and income that is received in India. After computing income under different heads, brought forward losses are set-off according to the provisions contained in Sections 70 to 80 of the

Indian Income Tax Act, 1961 resulting in gross total income. Deductions under Chapter VI-A (i.e., deductions under Section 80) are taken out of

gross total income netting in total income. The Act contains the provisions for carry forward of losses of previous years of the company. Minimum Alternate Tax Minimum Alternate Tax

has been introduced with the objective of bringing the “zero-tax” companies into the tax net. Zero tax companies were basically those companies, which, inspite of having earned substantial book profits and paying dividends, do not pay tax due to the various concessions and incentives provided under the Income tax, Act. MAT is levied as per the provisions of Section 115JB of Income Tax Act, 1961.

Minimum Alternate Tax is payable only if the tax payable on the income computed as per the other provisions of the Income Tax Act, 1961 (i.e., all provisions excluding Section 115JB that relates to minimum alternate tax) is less than 15 percent (plus surcharge and cess as applicable)

of book profits. Minimum Alternate Tax is payable to both Indian and foreign companies from the assessment years commencing on or after 1 April 2001.

For a company, which is a unit of the International Financial Services Centre and deriving its income solely in convertible foreign exchange, the MAT is levied at 9% (plus surcharge and cess as applicable) 14 14

<https://www.incometaxindia.gov.in/tutorials/10.mat-and-amt.pdf>

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Alternate Minimum Tax (AMT) Alternate Minimum Tax (AMT) is introduced as the extension of MAT for tax payers, other than companies. The provisions of MAT are applicable to a corporate taxpayer only. The provisions relating to AMT are applicable to non-corporate taxpayers in a modified pattern in the form of Alternate Minimum Tax, i.e., AMT. Thus, it can be said that MAT applies to companies and AMT applies to a person other than a company. The provisions relating to AMT are given in Sections 115JC to 115JF. The provisions of AMT will apply to every non-corporate taxpayer who has claimed deductions as under (i) Deduction under section 80H to 80RRB (except 80P), (ii) Deduction under section 35AD and (iii) Deduction under section 10AA. Thus, the provisions of AMT are not applicable to a non-corporate taxpayer who has not claimed any deduction under above discussed sections. The other provisions to be looked into are: The provisions of AMT shall apply to

an individual or a Hindu undivided family or an association of persons or a body of individuals (whether incorporated or not) or an artificial juridical person

only if the adjusted total income (discussed later) of such person exceeds ₹ 20,00,000.(Section 115JEE) The provisions of AMT shall apply to every other person (i.e., other than an individual or a HUF or an AOP/BOI or an artificial juridical person) irrespective of its income. Further the provisions of AMT are not applicable to a person who has exercised the concessional tax regime available under section 115BAC or section 11BAD. Rate of AMT In case of non-corporate taxpayer, AMT is levied @ 18.5% of adjusted total income (discussed later). Surcharge and cess as applicable will also be levied. However, AMT is levied @ 9% in case of a non-corporate assessee being a unit located in International Financial Services Centre and deriving its income solely in convertible foreign exchange. Surcharge and cess as applicable will also be levied. With effect from the Financial Year 2020-21, dividend income is taxed in the hands of the investor/shareholders. AS such, dividends will be taxed at normal tax rates as applicable except in case of: A resident individual being an employee of an Indian company or subsidiary engaged in IT, Entertainment, Pharmaceutical or bio-technology industry, who receives dividend in respect of GDRs issued by such company under ESOP scheme. Under such a case, dividend will be taxed at 10% without any deduction under Income Tax Act.

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Check Your Progress – 2 6. As per Section 2(68) of the Companies Act 2013,

what is the maximum limit on membership in a private company? a. 50 b. 100 c. 150 d. 200 e. 250 7.

According to which provisions of Income tax Act, 1961, brought forward losses are set-off after computing income under the different heads? a. Sections 70 to 80 b. Sections 60 to 70 c. Sections 70 to 75 d. Sections 75 to 80 e. Sections 80 to 85

8. The Competition Act, 2002 does not cover which of

the following areas? a. Prohibition of competitive agreements. b. Prohibition of abuse of dominant position. c. Regulation of combinations. d. Establishment of Competition Commission of India. e. Penalties for contravention of orders of Commission and non-compliance with directions.

9. Which of the following legislations was replaced by the FEMA Act? a. MRTP b. Companies Act, 1956 c. FERA d. Partnership Act, 1932 e. Income Tax Act, 1961

10. Which of the following is not a disadvantage of Partnership firm? a.

The life of the firm

depends upon the agreement between the partners. If any of them withdraws or meets with death, it may result in the dissolution of the firm. b. The work can be shared among the partners

c. Possible conflict between the partners is a threat to the company's existence. d. Personal liability of the partners is unlimited.

e. Its ability to raise funds is limited

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Activity 10.2 1. Describe the concept of One Person Company. Give two real time examples of such type of companies. 2. The launch of Reliance Jio by Reliance Communications and its offer of free services were viewed by its competitors as a case of predatory pricing, and were regarded as against the provisions of the Competition Act, 2002. Do you agree with the above statement? State the provisions of the Competition Act, 2002 in this regard.

10.10 Summary ? Financial Management is the effective and efficient management of funds to achieve the objectives of the organization. It includes planning, organizing, directing and controlling the financial activities such as procurement, allocation and financial control taking into account various risks involved in the process. ?

After Independence, the Government felt the importance of developing the country economically; and the first five-year plan was initiated in 1951 with focus on primary sector, and subsequent five-year plans with focus on other areas based on the Government priorities. The Planning Commission was formed in March 1950 based on the recommendations of the Economic Program Committee (EPC). ? The Planning Commission was replaced by NITI Aayog in 2015. NITI Aayog or National Institution for Transforming India Aayog is basically a policy think tank of Government of India and State Governments. Its primary job is to undertake long-term policy, design frameworks, take necessary initiatives for attaining faster development and monitor these activities. In Niti Aayog, the various sources of finance can be broadly segregated into short-term and long-term sources of finance. ?

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Public Finance Management PFM refers to the set of laws, rules, systems and processes used by sovereign nations (and sub-national governments), to mobilize revenue, allocate public funds, undertake public spending, account for funds and audit results. It encompasses a broader set of functions than Unit 10: Financial Management Process 59 financial management and is commonly conceived as a cycle of six phases-

Policy, Budget Formulation, Budget Approval, Budget Execution, Accounting and External Audit. ? Any Government/ business/ individual entity needs two types of funding - long-term funds and short-term funds. Long term funds are needed to set up the unit, diversification, expansion, modernization and similar capital expenditure investments. Similarly, these entities also need short-term funds for its day-to-day operations, also called working capital funds. ? Financial management for an individual or a family is called personal financial planning. One of the major benefits of financial planning is that it helps us to acquire, use, control and manage our financial resources most effectively. ? The important forms of business organizations are sole proprietorship, partnership and Joint Stock Company. ? One Person Company (OPC) is the company introduced for the first time in the Companies Act, 2013. This is in addition to a private company and a public company under this Act. An OPC means a company having only one person as its member. [Section 2(62) of the Companies Act, 2013] ?

Corporate investment and financing decisions are circumscribed by a government regulatory framework. The important elements of this framework are: (i) Industrial policy, (ii) Industrial licensing provisions and procedures, (iii) Regulation of foreign collaborations and investments, (iv) Foreign Exchange Management Act, (v) Competition Act, 2002, (vi) Companies Act, 1956, and (vii) SEBI. 10.11 Glossary

NITI Aayog or National Institution for Transforming India Aayog: It is basically a policy think tank of Government of India and State Governments. Its primary job is to undertake long-term policy, design frameworks, take necessary initiatives for attaining faster development and monitor these activities. Anti-competitive agreements are agreements made by an enterprise or association of enterprises or person or association of persons in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services, which causes or is likely to cause an appreciable adverse effect on competition within India Budget: A budget is an annual financial statement showing item wise estimates of expected revenue and anticipated expenditure during a fiscal year Budgetary process is estimating the availability of resources and allocating them to various activities based on pre-determined priority.

Block IV: Financial Management 60

Company: A company is a voluntary association of persons formed for the purpose of doing business, having a distinct name and limited liability. Competition Act, 2002 is framed

to promote the spirit of competition and harmonize the conflicts caused by the volatility of globalized markets.

Commercial Paper is a short term unsecured promissory note issued by highly rated corporates with a maturity period up to 180 days. Dated Government securities are long-term securities with a tenor up to 30 years. Dividend distribution tax is levied in addition to normal tax payable by a company. This tax should be payable by the company even if no income tax is payable by that company on its total income computed under the provisions of the Act.

Funds flow analysis: It is an important analytical tool for developing information to be used in financial decision making. It is a statement that explains the various sources from which funds are raised and used in various Assets. Government Security: It

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is a tradable instrument issued by the Central Government or the State Governments.

Masala bonds are bonds issued outside India but denominated in Indian currency i.e., rupee. Minimum Alternate Tax: It

is payable only if the tax payable on the income computed as per the other provisions of the Income Tax Act, 1961 (i.e., all provisions excluding Section 115JB that relates to minimum alternate tax) is less than 7.5 percent of book profits.

Navratna Companies are Public Sector Undertakings in India which have been given financial autonomy in 1997. There are nine such navratna companies. Non-Budgetary Activities are all the expenditures undertaken by the Government which are not routed through consolidated fund of the state, are outside the budgetary processes and not accounted for in the budget document. One Person Company: A type of company introduced for the first time in the Companies Act, 2013. This is in addition to a private company and a public company under this Act. An OPC means a company having only one person as its member. [Section 2(62) of the Companies Act, 2013]

Partnership: In this type of firm, the business is owned by two or more persons. They are partners in business and they bear the risks and reap the rewards of the business.

Personal Financial Planning: Financial management for an individual or a family unit is also called personal financial planning.

Unit 10: Financial Management Process 61

Sole Proprietorship: This type of concern is owned by a single person. The proprietor enjoys all the powers of taking and assuming risks for his/her concern.

Treasury bills are short term government securities with original maturities of less than one year and are presently issued in three tenors, namely, 91 day, 182 day and 364 day. 10.12 Self-Assessment Test 1. Describe the sources of funds for government undertakings. 2. What is a budget? What are budgetary and non-budgetary activities? 3. Discuss the various forms of business organizations and their relative merits and demerits. 4. Write a detailed note on the regulatory environment for corporate finance in India. 10.13

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Unit 10: Financial Management Process 63 10.14

Answers to Check Your Progress Questions 1. (e) Ensuring prompt payment of taxes The four major objectives of financial

management are (i) ensure regular and adequate supply of funds to the organization, (ii) ensure adequate returns to the shareholders,

(iii) ensure optimum utilization of funds and (iv) ensure safety on investments made. 2. (a) Niti Aayog With Niti Aayog in place, the

planning commission has ceased to exist and the allocation of funds to states is done by the Finance Ministry's Department of

expenditure in the new dispensation. 3. (d) Expenditure of rural infrastructure Expenditure on rural infrastructure is a budget

allocation. 4. (c) Budgetary process Budgetary process is estimating the availability of resources and allocating them to various

activities based on pre-determined priority. 5. (c) Tax revenue The tax revenue is the prominent source of funds for the state governments and this includes sales tax, excise, tax on goods, tax on vehicles, stamp duty, electricity duty, tax on passengers and land revenue, tax on professions, trade, selling and employment, entertainment duty and advertisement, road tax and tourist tax. 6.

(d) 200 As per Section 2(68),

a private company means a company which has a minimum paid-up capital of one lakh rupees or such higher paid-up capital as may be prescribed and by its articles

and limits the number of its members to two hundred. 7. (a) Sections 70 to 80

After computing income under the different heads, brought forward losses are set-off according to

the provisions contained in Sections 70 to 80 of the Indian Income Tax Act, 1961 resulting in gross total income. 8. (a) Prohibition of

competitive agreements The Competition Act, 2002 covers

the following: Prohibition of anti-competitive agreements; Prohibition of abuse of dominant position, Regulation of combinations,

Establishment of Competition Commission of India, Penalties for contravention of orders of Commission and non-compliance with

directions, Competition advocacy,

and Constitution of competition fund.

Block IV: Financial Management 64 9. (

c) FERA

The Foreign Exchange Regulation Act, 1973, regulated foreign investment in India. The Foreign Exchange Management Act (FEMA) replaced the Foreign Exchange Regulation Act (FERA) with effect from June 1, 2000. 10. (b) The

work can be shared among the partners The disadvantages of a Partnership

are: ? The life of the firm depends upon the agreement between the partners. If any of them withdraws or meets with death, it may result in

the

dissolution of the firm. ? Possible conflict between the partners is a threat to the company's existence. ? Personal liability of the partners is unlimited. ? Its ability to raise funds is limited.

Unit 11 Financial System – Indian and International Scenario

Structure 11.1 Introduction 11.2 Objectives 11.3 Functions Performed by a Financial System 11.4 Financial Markets 11.5 Introduction to Capital Markets 11.6 Government Securities Market 11.7 Financial Institutions 11.8 Functions of Reserve Bank of India 11.9 Functions of Commercial Banks 11.10 Financial Sector Reforms 11.11

Structure of

Financial System – International Scenario 11.12 Evolution of International Monetary System 11.13 Role of International Financial Institutions 11.14 International

Financial Instruments 11.15

Summary 11.16 Glossary 11.17 Self –Assessment Test 11.18 Suggested Readings/Reference Material 11.19 Answers to Check Your Progress Questions 11.1

Introduction

Unit 10

Financial

management process discussed how

Financial Management is the effective and efficient management of funds to achieve the objectives of the organization. It includes planning, organizing, directing, and controlling the financial activities such as procurement, allocation, and financial control taking into account various risks involved in the process. In the

unit, we discussed the short-term/long-term financial requirements of Governments/business entities/individuals. We briefly discussed what Public Finance Management is.

The financial system is one of the most important developments of the modern society. The phenomenon of imbalance in the distribution of capital or funds exists in every economic system. There are areas or people with surplus funds and there are those with a deficit.

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A financial system functions as an intermediary and facilitates the flow of funds from the areas of surplus to the

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A financial system functions as an intermediary and facilitates the flow of funds from the areas of surplus to the

Block IV: Financial Management 66

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areas of deficit. A financial system is a composition of various institutions, markets, regulations and laws, practices, money managers, analysts, transactions and claims and liabilities.

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A financial system is a composition of various institutions, markets, regulations and laws, practices, money

The financial system helps determine both the cost and the volume of credit. The system can affect a rise in the cost of funds which adversely affects the consumption, production, employment and growth of the economy. Vice-versa, lowering the cost of credit can enhance all the above factors in the positive direction. Thus we find that a financial system has an impact on the basic existence of an economy and its citizens.

This unit provides an overview of the financial system, and the role of financial markets and financial institutions in it. It also discusses the functions of the Reserve Bank of India, commercial banks and gives an overview of the International Financial System. 11.2

Objectives After reading through the unit, the student should be able to: ? Discuss the

functions performed by a financial system ? Explain the role of

financial market and financial institutions ? Describe the

primary, secondary markets in equities and other securities and government securities markets in India ? Describe the functions of various

All India Development Banks and Investment Institutions in India ? Identify the functions of

the RBI and Commercial banks ? Outline the financial sector reforms introduced in India ? Discuss the concept of Payment banks and Small banks ? Describe the structure of International Financial System ? Trace the evolution of International Monetary System ?

Outline the various International Financial Institutions and Instruments 11.3

Functions Performed by a Financial System A Financial System is the principal medium through which savings of households are converted into investments. An understanding of the financial system and its functions is vital for a finance manager who has to take financial decisions.

The functions performed by a financial system are: 11.3.1 Savings Function

As already stated, public savings find their way into the hands of those in production

through the financial system. Financial claims are issued in the money and capital markets, which promise future income flows. The funds with

Unit 11: Financial System – Indian and International Scenario 67

the producers result in the

production of better goods and services, thereby increasing society's living standards. When the savings flow declines, however, the growth of investment begins to fall. 11.3.2 Liquidity Function Money in the form of deposits offers the least risk of all financial instruments. But its value is most eroded by inflation. That is why one always prefers to store the funds in financial instruments like stocks, bonds, debentures, etc. The compromise one makes in such investments is that (i) the risk involved is more, and (ii) the degree of liquidity, i.e., conversion of the claims into money is less.

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The financial markets provide the investor with the opportunity to

liquidate the investments. 11.3.3

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Payment Function The financial system offers a very convenient mode of payment for goods and services. The cheque system, credit card system et al. are the easiest methods of payments.

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financial system offers a very convenient mode of payment for goods and services. The cheque system, credit card system et al. are the easiest methods of payments. The cost and time of transactions are drastically reduced.

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In India, the cheque system of payment is widely practiced. The

credit card system is widely used to pay for consumption expenditure. 11.3.4

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Risk Function The financial markets provide protection against life, health and income risks.

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financial markets provide protection against life, health and income risks. These

are accomplished through the sale of life and health insurance and property insurance policies.

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The financial markets provide immense opportunities for the investor to hedge himself against or reduce the possible risks involved in various investments. 11.3.5

Policy Function India is a mixed economy. The government intervenes in the financial system to influence macroeconomic variables like interest rates or inflation. Higher inflation is the hurdle to economic growth.

To control higher inflation, the government through the Central Bank, changes the

bank rates, repo rates and CRR. Modern day economies require huge sums of money for investment in capital assets (land, equipment, factory, etc.) which are then used for providing goods and services. The funds required are so huge that it is not possible for a single investor to provide them. By selling financial claims like stocks, bonds, etc., the required funds can be quickly raised from a variety of investors. The business firm/government issuing such a financial claim, then hopes to return the borrowed funds from expected future inflows. Indeed, we see that the financial markets within the financial system have made possible the exchange of money at current value for future value and transformation of savings into investments, so that production and income grow.

Block IV: Financial Management 68 11.4

Financial Markets

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A financial market can be defined as the market in which financial assets are created or transferred.

Financial assets

represent a claim to the payment of a sum of money sometime in the future

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and/or periodic payment in the form of interest or dividend.

Financial markets are sometimes classified as primary and secondary markets. But, more often financial markets are classified as money markets and capital markets. The distinction between the two markets is based on the differences in the period of maturity of the financial assets issued in these markets. Money market deals with all transactions in short-term instruments (with a period of maturity of one year or less like treasury bills, bills of exchange, etc.) whereas capital market deals with transactions related to long-term instruments (with a period of maturity of above one year like corporate debentures, government bonds, etc.) and stock (equity and preference shares). 11.4.1 Money

Markets

One of the important functions of a well-developed money market is to channel savings into short-term productive investments like working capital.

Call Money Markets, Treasury Bills Market, and Markets for Commercial Paper and Certificates of Deposit are

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some of the examples of a Money Market. Call Money Market The call money market forms

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Money Market. Call Money Market The call money market forms a part of the national money market, where day-to-day surplus funds, mostly of banks, are traded.

The call money loans are of very short-term in nature and the maturity period of these loans varies from 1 to 15 days. The money that is lent for one day in this market is known as 'call money', and if it exceeds one day (but less than 15 days), it is referred as 'notice money'. In this market, any amount could be lent or borrowed at a convenient interest rate, which is acceptable to both the borrower and lender. These loans are considered as highly liquid, as they

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are repayable on demand at the option of either the lender or the borrower.

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at the option of either the lender or the borrower. The interest rate

on the call money borrowings

is known as the call rates. Unlike in the case of other short-term and long-term rates, the call rate is expected to freely

reflect the day-to-day availability of funds. These rates vary

highly from day-to-day, often from hour to hour

based on demand and supply of the money and liquidity position of the markets. Call

money is borrowed from the market to meet various requirements of the

commercial

bill market and banks. The commercial bill market borrows call money for short periods to discount commercial bills. Banks borrow in

the

call market to fill the temporary gaps or mismatches that arise as the banks normally lend out the deposits they mobilize

and to meet the Cash Reserve Ratio (CRR) requirements. Thus,

call money essentially

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serves the purpose of equilibrating the short-term liquidity position of banks.

Unit 11: Financial System – Indian and International Scenario 69

Commercial Papers (CPs), and Certificate of Deposits (CDs) are money market instruments launched in

the early nineties, and the market for these instruments is

not well-developed in India when compared to foreign countries. Commercial Papers (CP) Based on the recommendations of the

Working Group on Money Markets, the RBI introduced Commercial Paper (CP) in 1990 enabling

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highly rated corporate borrowers, to diversify their sources of short-term borrowings and to provide an additional instrument to investors.

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highly rated corporate borrowers, to diversify their sources of short-term borrowings and

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provide an additional instrument to investors. Commercial Paper (CP) is an unsecured usance money market instrument issued in the form of a promissory note

at a discount,

and is transferable by endorsement and delivery and is of fixed maturity.

CP may be issued to and held by

individuals, banking companies, other

corporate bodies registered or incorporated in India and unincorporated

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bodies, Non-Resident Indians (NRIs), and Foreign Institutional Investors (FIIs). However, investment by FIIs would be within the limits set for their investments by Securities and Exchange Board of India (SEBI).

When NRIs subscribe to CP issue, the conditions regarding non-repatriability and non-endorsability are indicated on the CP.

Certificates of Deposits (CD) Certificates of Deposit (CDs) were introduced in India in 1989 on the

basis of the suggestions given by the Vaghul Committee. With the introduction of CDs, the market for short-term instruments further

expanded with the investor getting more flexibility to invest their short-term surplus funds. The popularity of Certificates of Deposits

lies in the fact that they are low risk category investment option and stand next to T-bills in safety of investment. Certificate of

Deposit (CD) is a secured, negotiable promissory note which is short term in nature. The certificates

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are issued at a discount to the face value and the discount rate

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are issued at a discount to the face value and

depends on the negotiation

between the issuer and the investor.

Scheduled commercial banks, selected all India financial institutions are allowed by RBI to issue CDs for raising short-term funds.

Regional Rural Banks (RRBs) and Local Area Banks (LABs) are not allowed to issue these instruments.

The minimum amount of a CD an investor can subscribe should not be less than ` 1 lakh and should be multiple of ` 1 lakh thereafter.

They are issued to individuals, corporations, companies, trust, funds, etc. NRIs can purchase the Certificate of Deposits on non-repatriable basis. This information should be clearly mentioned on the certificate and cannot be transferred to another NRI through the secondary market. CDs may be issued at a discount on face value with the issuing bank/FI having the flexibility to state the discount/coupon rate. Banks/FIs are also allowed to issue CDs on floating rate basis.

Table 11.1 provides the details of the quantum of issue of Certificate of Deposits by Commercial Banks in India between July, 2020 to July, 2021.

Block IV: Financial Management 70

Table 11.1: Certificates of Deposit Issues by Scheduled Commercial Banks between July,2020 July 2021 Item 2020 2021 July 31 June 18 July 2 July 16 July 30 1 2 3 4 5 1

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Amount Outstanding (₹ Crore) 104705.00 68209.42 69,299.52 64,586.90 64,304.10 1.1 Issued during the fortnight (₹ Crore) 1292.97 6209.13 8817.62 270.74 950.89 2 Rate of Interest (per cent) 3.39-4.45 3.44-4.11 3.44-4.21 3.68-4.21 4.05-4.85		

Source: https://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/27T_BULL0921714243CF244C43DEBBE_B76E2B1725442.PDF

Money Market Mutual Funds (MMMFs) The benefits of developments in the various instruments in the money market like call money loans, treasury bills, commercial papers and certificate of deposits were available only to the few institutional participants in the market. The main reason for this was that huge amounts were required to be invested in these instruments, the minimum being ` 10 lakh, which was beyond the means of individual investors.

The purpose of establishing MMMFs was to help the small investors. MMMFs are those mutual funds that invest mostly in money market instruments. Such money market instruments are of very high quality and of very short maturities. MMMFs can be set up by commercial banks, RBI and public financial institutions either directly or through their existing mutual fund subsidiaries.

Only individuals can subscribe to these instruments as per the stipulations.

Activity 11.1 a. Visit the RBI website and gather information on the call money market rates. What do they indicate?

Unit 11: Financial System – Indian and International Scenario 71

b. Depict the inter-relationship among the functions of a financial system in the form of a flow chart. c. Evaluate the features of any five money market mutual funds operating in India. 11.5

Introduction to Capital Markets The capital market provides the resources needed by medium and large-scale industries for investment purposes while the money market provides resources for working capital needs. As such, while money market deals in short-term sources of funds (maturity period of which is less than 1 year) capital market deals in long-term sources of funds (with more than 1 year maturity). Thus, the capital market acts as an institutional mechanism for transferring the long-term funds from the hands of the savers to the hands of those who employ them for productive purposes. It serves as an intermediary which brings together entrepreneurs, helps in initiating entrepreneurial activity by arranging financial resources and savers, individuals or institutions, who are looking for viable investment opportunities. Structure of the Capital Market The structure of the Capital Market is shown below in Figure 11.1:

The capital market consists of the primary markets and the secondary markets and there is a close link between them. The primary market creates

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long-term instruments through which corporate entities borrow from the capital market.

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long-term instruments through which corporate entities borrow from the capital market.

But secondary market is the one which provides liquidity and marketability to these instruments. These markets interact. If the secondary market is active and buoyant, it enables the corporate entities to enter the new issue market or the primary market and raise funds. The depth of the secondary market depends upon the activities of the primary market because it is only when more corporate entities enter the market and raise funds through the market that more instruments are available in the secondary market for the purpose of improved activities in this market. 11.5.1

Primary Market To meet the financial requirements of their projects, companies raise capital through issue of securities (shares and debentures) in the primary market.

Block IV: Financial Management 72

Capital issues of the companies were controlled by the Capital Issue Control Act, 1947. Pricing of the issues was determined by the Controller of Capital Issues. The main purpose of control on capital issue was to prevent the diversion of investible resources to non-essential projects. Though the necessity of retaining some sort of control on issue of capital to meet the above purpose still exists, the CCI was abolished in 1992 as the practice of Government control over capital issues as well as overpricing of issues has lost its relevance in the changed circumstances.

SEBI The CCI Controls on Issue of Capital by the companies have been substituted by the transparent and simplified guidelines issued by the Securities Exchange Board of India under the SEBI Act, 1992.

Figure 11.1: Structure of Capital Market

Source: ICFAI Research Center

Unit 11: Financial System – Indian and International Scenario 73

Functions and Powers of SEBI Prior to 1988, the growing population of investors exposed the stock markets to a plethora of malpractices resorted to by companies, brokers, merchant bankers, investment consultants and several other agencies who were involved in the issue of securities. This resulted in a decrease in the investor confidence and magnified their grievances. The government and the stock exchanges were clueless because the existing legal framework was not

adequate. Towards this end, a need was felt for a regulatory body, which was satisfied with the establishment of SEBI by the government in April 1988. It was given legal status in 1992, as a supervisory body to regulate and promote the securities market to:

- ? Promote fair dealings by the issuers of securities and ensure a market place where funds can be raised at a relatively low cost.
- ? Provide a degree of protection to the investors and safeguard their rights and interests, so that there is a steady flow of savings into the market.
- ? Regulate and develop a code of conduct and fair practices by intermediaries in the capital market like brokers and merchant banks to make them competitive and professional.

To carry out its functions SEBI has been given various powers which were previously vested with the Central government. These include:

- ? Power to call for periodical returns from Stock Exchanges, subject to the fulfillment of certain criteria.
- ? Power to call upon the Stock Exchange or any member of the exchange to furnish relevant information.
- ? Power to appoint any person to make inquiries into the affairs of the Stock Exchange.
- ? Power to amend byelaws of the

Stock Exchange.

- ? Power to compel a public company to list its shares in any Stock Exchange.

Guidelines as per SEBI and Companies Act, 2013 SEBI has issued elaborate guidelines on matters relating to public issues, rights issues, bonus issues, issue of debentures, underwriting, private placement, pricing of issues, etc. These guidelines virtually affect all activities relating to capital issues. Under the new guidelines, no prior approval of SEBI is required by the companies for raising capital through public issues and

rights issues in the capital market, subject to the fulfillment of certain criteria. A company, while raising its capital through issues in the capital market must give due regard to the Guidelines and clarifications issued by SEBI and the provisions of the Companies Act, 2013.

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As far as the Companies Act, 2013 is concerned, capital issued by a company should comply with the provisions relating to prospectus, allotment, issue of shares at premium/discount, further issue of capital, etc. As per the Companies Act, all application forms for shares or debentures should be accompanied by a memorandum containing salient features of a prospectus like general information of the company, terms and particulars of the issue, company's management, risk factors as perceived by the management, etc., which may possibly have a bearing on the assessment of the soundness of the proposition of the company in connection with which the public issue is offered.

Under

the SEBI guidelines, companies are allowed to issue capital provided the issues are in conformity with the published guidelines relating to disclosure and other matters relating to investors' protection. Types of Issue 15 A company can raise its capital through issue of shares and debentures by means of, ? Public issue ? Rights issue ? Bonus issue ? Private placement ? Bought-out Deal Public Issue: Public issue is the most popular method of raising capital and involves raising of funds directly from the public. Rights Issue: Rights issue is the method of raising additional finance from existing members by offering securities (shares and debentures) to them on pro rata basis. A company proposing to issue securities on rights basis should send a 'letter of offer' to the shareholders, giving adequate disclosure as to how the additional amount received by the issue is used by the company. Bonus Issue:

Bonus shares are shares issued by companies to existing shareholders out of accumulated profits or free reserves. They are issued as fully paid shares and since the shareholders do not pay, they are also referred to as "free shares".

Bonus shares are issued in the ratio of existing shares held.

Private Placement: Private Placement Market (PPM) financing is the direct sale by a public limited company or private limited company, of private as well as public sector, of its securities (shares and debentures) to a limited number of sophisticated investors like LIC, GIC, State Finance Corporations and Pension and Insurance Funds. The intermediaries are credit rating agencies and trustees (example, ICICI) and financial advisors such as merchant bankers. 15

The various types of shares and debentures have been discussed in detail in the unit on Sources of Long-Term and Short Term Finance.

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Private companies that do not wish to disclose information to the public, seek this type of market. Public limited companies, too small to finance

a public issue as it is costly due to various statutory and non-statutory expenses, can resort to this type of market. And the maximum time-frame required for private placement market is only 2 to 3 months. Private Placement can be made out of the promoter's quota, but it cannot be made with unrelated investors.

Exhibit 11.1 gives example of issue of bonds through the private placement route.

Exhibit 11.1: Example of

58%

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Private Placement Bank of India, in September 2021 raised ₹ 1,800 crore by issue of Basel III compliant bonds Tier –II bonds on a private placement basis

These bonds have a tenure of 10 years with a 5 year call option and carry a coupon rate of 7.14 percent. Before this issue, the Bank had already raised ₹1,352 crore through the issue

100%**MATCHING BLOCK 70/173****W**

of Basel-III compliant additional tier-I bonds on a private placement basis.

Source: <https://www.livemint.com/>

88%**MATCHING BLOCK 71/173****W**

industry/banking/bank-of-india-raises-rs-1-800-cr-through-basel-iii-compliant-bonds-11633006728250.

html

Bought-out Deals: A small project costing around ` 5-6 crores of rupees

finds it costly to go in for a public issue which would eat up 20% of project funds. Bought-out Deals come to the rescue of the promoters of such a project. What exactly is a Bought-out Deal (BOD)? In its simplest form, a company initially places its equity shares, which are to be offered to the public at a later date, with a sponsor/merchant banker, who in turn offloads the shares at the appropriate time. In a direct offer the merchant banker (or sponsor) is a conduit through whom a company routes shares to the public, whereas in a BOD, the sponsor is also an intermediate investor who buys stakes in the company and disinvests in favor of the public at an appropriate time. 11.5.2

Secondary Market The secondary market is a part of the capital market wherein the securities already issued by entities (securities already issued) are traded. The major benefit of a secondary market to the

investors is that it provides

liquidity to the long-term securities held by them by providing

a ready

market for these securities. The secondary market operates through the medium of stock exchanges. These exchanges regulate the trading activities in this market and

uphold the safety and integrity of

the dealings.

India has a long tradition of trading in securities going back to nearly 200 years. The first Indian stock exchange established at Mumbai in 1875 is the oldest exchange in Asia. The main objective was to protect the character, status and interests of the native share and stock brokers.

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National Stock Exchange The National Stock Exchange is India's latest bourse.

It is a computerized exchange

not confined to scattered pockets, and has a national reach through satellite linkage. Like the BSE, only members conduct transactions, but professionals who do not have a stake in the system run it. The idea of forming NSE was conceived by the late Mr.

M.J. Pherwani who was then the Chairman of National Housing Bank. The trading on NSE commenced with debt instruments from June 30, 1994. The NSE launched its equity market segment on the 3rd of November, 1994. The trade was for 100 shares of Reliance. On this day during the three hour session 1,498 trades were executed in 200 securities with a value of ₹ 9

crore. The main objectives of the NSE are to provide speedy transactions, fast settlements and to benefit the small investor who often finds it difficult to sell shares at BSE.

Trading System Trading on all stock exchanges was being carried out by "public outcry" in the trading ring. This was an inefficient system and also resulted in lack of transparency in trade.

Screen based trading received a big boost with the setting up of the National Stock Exchange. NSE provided nationwide access to investors by setting up trading terminals all over the country. These terminals were networked through satellite links.

Since the eighties, there has been an unprecedented growth of the stock markets. The number of stock exchanges in the country have increased from 8 in 1980 to 24 in 1993 and 17 in 2016.

By 2021, there are 9 stock exchanges operating in the country 16 .

The present stock exchanges have a much wider role to play wherein protection of the investors' interests becomes the paramount concern. The stock market

in India is regulated by the Central Government under the Securities Contracts (Regulation) Act, 1956. Under this Act, the Government has the powers to supervise and control the stock exchanges and also keep a check on the governing body and supersede it if any irregularities are found to have been committed.

The stock market is a pivotal institution in the financial system. A well-ordered stock market performs several economic functions like translating short-term and medium-term investments into long-term funds for companies, directing the flow of capital in the most profitable channels, etc. 16

<https://www.sebi.gov.in/stock-exchanges.html>

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To give a boost to stock market the government announced certain favorable policy measures like: i. Establishing SEBI. ii. Taking steps to encourage foreign investment in the

securities market. iii. Starting electronic linkage of 5 large stock exchanges. iv. Giving recognition to more stock exchanges. vi.

Allowing investments by Foreign Institutional Investors (FIIs). Until the entry of the FIIs, the domestic financial institutions were the major players in the market along with some wealthy individuals and investment institutions (mutual funds). Though small investors also participated in the market very actively until the scam, they have deserted the market since then. The FIIs, with their vast resources, are now among the biggest players in the market and the government has been taking measures from time to time to encourage them to bring in foreign capital. This helps to perk up the secondary market. The FIIs, however, are subject to certain regulations made by the SEBI and also some other statutes: ? FIIs would be required to obtain an initial registration with SEBI before investment. Along with the application to SEBI, FIIs would also be required to file an application addressed to RBI for obtaining various permissions under the FEMA, 1999. ?

Portfolio investments in primary or secondary markets, subject to a ceiling of 30 percent of issued share capital for the total holdings of all FIIs in any one company. Similarly, the holding of single FII in any company should not exceed 10 percent of total issued share capital. ?

SEBI shall take into account the track record of the FII, the additional criteria that are relevant for granting registration. ? There is no restriction on the amount of investment and no lock-in period. ? They are required to allocate their total investment in the ratio of 70:30 between equities and debentures. ? FIIs cannot engage in short sales. ? Short-term capital gains arising out of transfer of securities are taxed at 30%, and interest and dividend at 20%. ? Disinvestment should be through stock exchanges in India, through a custodian (approved by SEBI).

The fully automated trading system enabled market participants to login orders, execute deals and receive online market information. The competition from NSE forced the regional stock exchanges including BSE to switch over to screen based trading. The NSE trading system is order driven. In an order driven environment, the system captures all the orders and matches them with each other to execute the transaction. A quote driven system is based on the

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market making concept (dealer giving two way quotes) and the order logged in is matched against the best quote given by the market maker. BSE Online Trading (BOLT) is a mixture of both quote driven and order driven system as the system permits both

jobbing and direct matching of orders. Depositories One of the major drawbacks

of Indian capital market was that the securities were held in the form of certificates. This led to problems in physical storage and transfer of securities. There was also the risk of bad delivery for the buyer. The transaction costs were also higher due to physical movement of paper and the incidence of stamp duty. National Securities Depository Ltd. (NSDL) was set up in 1996 as India's first depository.

A depository is an entity, which holds the securities in electronic form on behalf of the investor. This is done through

dematerialization of holdings at the request of the investor. Dematerialization is a process by which physical certificates of the

investor are destroyed and an equivalent number of securities are credited to his account. This also enables transfer of securities by

book entries. The risk of bad deliveries is also eliminated. The transaction costs are also reduced due to less flow of paper and transfer of securities through depository does not attract stamp duty. Further the depository also handles all the corporate actions like exercising for rights, collection of dividends, credit for bonus, exercising of warrants, conversion option, etc., on behalf of the

investor. SEBI has made it mandatory for institutional investors to have their holdings in dematerialized form. Clearing Mechanism The clearinghouses attached to the stock exchanges functioned only as conduits to delivery of securities and money. The default risk by the counterparty in the transaction remained. The NSE was the first stock exchange to set up a clearing corporation. The National Securities Clearing Corporation (NSCC) assumes the counterparty risk in all trading deals made on the exchange. NSCC acts as the counterparty for all the trades, and bears the default risk in the deal. NSE created a special Trade Guarantee Fund for this purpose and any loss due to default would be met from its corpus.

Carry Forward System Earlier,

Carry Forward System Earlier,

the Indian Stock Exchanges had been an amalgam of cash market and forward market. The prices of the scrips on the exchange did not reflect their 'true' price in the underlying cash market. Furthermore, there was indiscriminate and rampant speculation in the market. Defaults were common and other members were forced to "accommodate" the defaulting member. Often, the defaults had a snowballing effect and the entire market would be in

Unit 11: Financial System – Indian and International Scenario 79

the throes of a major payment crisis. This frequently resulted in the

closure of the exchanges for a few days. In order to curb the prevailing malpractices, SEBI banned carry forward transactions on all stock exchanges

in 1993. Later, based on the recommendation of the committee chaired by G.S. Patel - which worked out the modalities to re-introduce the system -

a modified carry forward system was introduced. The badla procedure was also streamlined. Again the system of carry forward of positions was banned from July 2, 2001. In order to give the market adequate time to orderly unwind the positions, the board recommended a transitional mechanism. As per the mechanism, all outstanding deferred positions in the current settlement would be compulsorily liquidated by September 3. The board also approved

the

introduction of options on individual scrips from July 2. Introduction of other derivative products to introduce the rolling settlement in the additional 251 scrips from July 2 was reiterated, thereby bringing the total number of scrips to 441. Further, it was decided that all scrips listed on all the stock exchanges should be traded only under rolling settlement mode, with effect from January 2, 2002, and

that no scrip shall be traded on weekly settlement basis.

Exhibit 11.2 discusses the advantages of the rolling settlement. Exhibit 11.2:

Advantage Rolling The rolling settlement has many virtues. One, it reduces speculation and arbitrage in scrips as settlement occurs on a daily basis. Thus, there would be

an

increase in delivery-based transactions, reducing the speculation currently existing by way of carry forward of position in various scrips. Apart from this, shifting position from one stock exchange to another will reduce, which in turn will eliminate arbitrage opportunities in scrips. Two, it reduces pricing glitches and manipulation, and explores a better price discovery process. With the rolling settlement in place, all open positions at the end of each day would come up for delivery, thereby improving the quality of cash market transactions. Thus,

the price formation process on a daily basis would be improved, thereby resulting in the

improved price discovery process. Three, it reduces end of settlement period pressure as shares are delivered and cash is paid every day instead of weekly. Thus, the rolling settlement spreads the delivery and payment throughout the week. Four, it narrows the bid-ask spreads, reduces the settlement risk and eliminates the need to synchronize the settlement dates on NSE and BSE, or for that matter across the exchanges. In addition, of course, with the implementation of a Rolling Settlement investors will be benefited, as settlement will not take long and the prices an investor pays or receives will be closer to the market price. Securities and money will be transmutable.

Source: ICFAI Research Center

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With regard to

settlement system, at present Indian Stock Exchanges are working on T + 2 rolling settlement system. Under T + 2 rolling settlement system all trades executed on a day are netted and only net obligation

is

to be settled by way of delivery or payment. In case of sale of shares, the seller is required to give the delivery by 1.30pm on T + 1 day to the depository participant. The DPs execute pay-in instruction by 10.30 A.M. on T + 2. The depository transfers the securities to the clearing house/exchange/ clearing corporation by 11 AM on T + 2 day. The clearing house/exchange/clearing corporation executes the payout of securities and funds latest by 1.30 P.M on T + 2 to the depositories and clearing banks and the depositories and the clearing banks in turn complete the process by 2.30 P.M on T + 2.

In September 2021, SEBI came up with a decision

76%

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to allow stock exchanges to offer T+1 trade cycle instead of T+2 cycle

to faster the settlement process. This will be effective from Jan 1, 2022, though the new trade cycle will not be mandatory. The change is likely to be advantageous to retail investors, who will be able secure access to cash and securities much sooner 17 .

The Settlement Procedure at NSE The NSE has a computerized trading mechanism. The mechanism is hooked nationwide via satellite to increase the scope and depth of the market. The automated environment, moreover ensures that all the orders floating in the system whether they are best buy or best sell quotes are available on the system. Each trading member of NSE has a computer located in his office wherever that may be in India. The computer is connected to the central computer system at NSE, by a satellite link using VSAT (Very Small Aperture Terminals). During the trading time, the member can go on entering the buy or sell orders with the best price and the time-frame within which he wants his orders to be executed. The computer will bear the various orders and within 30 seconds the transaction is executed and the unmatched orders are stored in the memory and executed when they are matched. Thus the role of jobbers is eliminated. The trading time on NSE is from 9.15 A.M. to 3.30 P.M. NSE trading system allows flexibility while placing an order, allowing brokers to place limits on price or on the order or even on the time-frame. The trading member can break large lots into smaller lots or cancel the outstanding orders in one go. The computer sorts out orders on the basis of price-time priority, i.e., sorts out orders as and when they are received in terms of the price of each security and the time entered. 17

<https://www.livemint.com/market/stock-market-news/sebi-to-shorten-trade-settlement-cycle-optional-for-stock-exchanges-11631029025665.html>

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Protection

of Identity of the Investor Till

the transaction is executed, the identity of brokers is not disclosed. As the participants' identity is protected, the trading member can even enter high volume transaction. Settlements The settlement for debt is to take place via a book entry transfer in a depository. The book entry transfer system is to operate similar to a bank passbook. The accounts would be maintained against each member, detailing securities held in the

member's

name. The Central Depository In the Central Depository the funds and securities position would be debited/credited through electronic book entry transfers, which are expected to speed up payments. Each member is to have a passbook account in the depository where the securities deposited in the members' name is recorded, by electronic book entry transfer. At the end of each day's transaction the computer generates a report of matched transactions and the net positions of each trading member.

Check Your Progress – 1 1.

Which of the following is not a

function performed by a financial system? a. Savings function b. Liquidity function c. Risk function d. Social function e. Policy function 2.

Which is/are the essential feature(s) of a Call Money Market? a. Maturity periods of 1-15 days b. Market determined interest rates c. Low liquidity d. High agency costs e.

Maturity periods of 1 -15 days and market determined interest rates 3. Which of the following

90%

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is an unsecured usance money market instrument issued in the form of a promissory note

90%

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023E2430_Financial Markets and Institutions.pdf (D165201762)

is an unsecured usance money market instrument issued in the form of a promissory note

at a discount,

and is transferable by endorsement and delivery and is of fixed maturity?

a. Certificate of deposit b. Treasury bill c. Commercial paper d. Money Market Mutual Fund e. Call Money Market

Block IV: Financial Management 82 4.

A process by which physical certificates of the investor are destroyed and an equivalent number of securities are credited to his account

is known as a. Demonetization b. Securitization c. Dematerialization d. Computerization e. Remonetization 5. Which of the following is not a power vested with SEBI? a.

Power to call for periodical returns from Stock Exchanges subject to the fulfillment of certain criteria. b. Power to call upon the Stock Exchange or any member of the exchange to furnish relevant information. c. Power to appoint any person to make inquiries into the affairs of the Stock Exchange. d. Power to amend Companies Act. e. Power to compel a public company to list its shares in any Stock Exchange. 11.6

Government Securities Market In the previous unit, we have understood that

100%**MATCHING BLOCK 76/173****SA**

mangal . Intoduction to Financial Markets & In ... (D22478819)

a government security is a tradable instrument issued by the Central Government or the State Governments.

Such securities, called treasury bills, are short term with

82%**MATCHING BLOCK 77/173****SA**

mangal . Intoduction to Financial Markets & In ... (D22478819)

original maturities of less than one year. The long-term Government bonds or dated securities have original maturity of one year or more. In India, the Central Government issues both treasury bills and bonds or dated securities 11.6.1

Types of Government Securities The term 'government securities' encompasses all bonds and treasury bills issued by the Central Government, State Governments, and other entities like corporations, municipal authorities and companies wholly owned by the government for the purpose of raising funds from the public. These securities are usually referred to as 'gilt-edged' securities as repayments of principal as well as interest are totally secured, being the first charge on the nation's purse. Hence, the Central Government securities are considered as safest claims. Dated Securities The government securities have been issued with maturities ranging from 3 to 31 years since independence. In

the

early '90s the average maturity period was shortened to 10 years by RBI. They can be classified into three categories depending upon their maturities viz., long-dated, medium-dated and short-dated. Long-dated securities have maturities exceeding 10 years from the issue date, medium-dated securities have maturities ranging from 5 to 10 years and short-dated securities are those which mature within 5 years.

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Depending upon the issuing body, such securities could be bifurcated into five types viz., ? Central Government securities. ? State Government securities. ? Securities guaranteed by

the

Central Government for All India Financial Institutions like IFCI, etc. ? Securities guaranteed by

the

State Government for state institutions like state electricity boards and housing boards. ? Treasury bills issued by RBI. Government securities could be held in three forms viz., i. Stock Certificates ii. Promissory Notes iii. Bearer Bonds Stock Certificates When public debt is issued in the form of stock, the owner gets a certificate specifying that he is a registered holder in the book of the Public Debt Office (PDO). The Certificate indicates the interest rate, interest due dates and

the

face value of the stock. A stock certificate is not transferable by endorsement. Transfer can take place only by means of a transfer deed upon the execution of which the transferee's name is substituted in the place of the transferor in the books of the PDO. Such transfer deed requires no stamp duty. A stock certificate is, thus, completely secure against loss by fire, theft, etc. and the title of the holder is not exposed to the risks which are attached to

the

holdings in negotiable securities. Interest payments are through interest warrants issued by the PDO to the domicile of the holder or a specified local office of the RBI or any branch of the agent bank conducting government securities business in India. Repayments of principal are also carried out in a similar fashion.

Promissory Notes Promissory Notes contain a promise by the President of India, or the Governor of the State for payment to the holder, the consideration along with interest. These are negotiable instruments payable to the order of specified persons and transferable by endorsement made in the boxes printed on the reverse of the notes. Bearer Bonds Bearer bonds certify the bearer for entitlement to the specified sum along with interest payable by interest warrants attached along with the bonds. Such bonds are transferable by mere physical delivery.

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Others Normally in the money market, government securities are held in the form of stock certificates. Besides these principal forms of government securities, there are other types of securities which are floated by the government from time to time. They are: i.

Treasury Bills ii. National Defense/National Savings/National Deposit Certificates iii. Deposit Certificates iv. Annuity Certificates v.

Annuity Deposit Certificates vi. Zamindari Abolition Compensation Bonds and Rehabilitation

Grant Bonds

vii. Social Security Certificates viii. Capital Investment Certificates. 11.6.2 Market for Government Securities

The market for government securities comprises

of:

Primary Market Reserve Bank of India is given the task of managing the public debt in the economy. It therefore regulates the issues by various issuing bodies since all of them have to tap the same market. It considers aspects such as – Quantum of Issue: The government of India declares its quantum of borrowing in its budget statement. They are issued by the RBI on behalf of GOI to finance the government's deficit and public sector development programs. Timing of Issue: Auctions are usually timed during periods of high liquidity to raise the maximum amount at the best price. The budgeted amount of issues in a given year are raised through a number of tranches that year to avoid flooding of securities in the market at one time

Terms of Issue: The terms of issue involve aspects such as coupon and maturity terms and normally the issues adhere to the long-term yield curve drawn by RBI for all government securities.

Investors: The major categories of investors in primary markets for government securities are: i. Commercial banks ii. Financial Institutions (FI) iii. Large corporate bodies iv. Reserve Bank of India v. Foreign Institutional Investors.

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Secondary Market The secondary market in government securities was a few years back quite narrow and dominated by a few institutions and commercial banks. However, in

the

early '90s the market has turned fairly active with various trading banks and some brokers quoting two-way prices which has imparted liquidity to this money market instrument. The secondary market for securities is akin to the call market with major business being concentrated done in Mumbai. RBI approved brokers are permitted to transact business in securities with banks, institutions and RBI. Transactions are effected in spot as well as in futures for outright sale/purchase as well as for 'ready forwards'. Settlement Procedure ? RBI acts as the depository and maintains SGL account for various banks and financial institutions. ? If the investor does not have SGL account, then it needs to open a constituent account with any registered bank authorized by RBI for the purpose. ? Transfer is through book entry method in SGL account maintained at PDO. ? Brokerage is 0.01 percent, but is negotiable i.e., it can be taken only from buyer, or seller, or from both. Security deals are carried out on ex-interest basis as per the byelaws of the various stock exchanges. This has also led to 'voucher trading' in the securities market. The amount of income tax deductible at source on the accrued interest income of government securities is popularly referred to as 'voucher'. Thus, in a securities transaction, the seller is entitled to receive from the buyer the quoted price plus interest accrued till date, as reduced by the income tax deductible at source on such interest. Such amount deducted on a pro rata basis is retained by the buyer, on the grounds that interest received by him on the due date would be after deduction of income tax. The buyer receives the tax certificate in respect of tax deduction on the interest income which could be set-off against his tax liabilities. The seller on the other hand does not receive such tax benefit as he does not get any Tax Deducted at Source (TDS) certificate. Banks and institutions find it advantageous to purchase securities around interest dates to avail themselves of the voucher benefit and subsequently unload. The RBI, being fully exempt from tax, does not stand to lose as seller. Though voucher trading is not a desirable practice it activates the securities market to a certain extent. The RBI is doing its best to curb voucher trading by fixing switch quotas for banks and brokers, suspending trading in a scrip before the interest due date, etc.

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Investors The major players in the secondary market are the commercial banks, the financial institutions, the brokers and the RBI. The yields on government securities are low and this prevents many aggressive mutual funds, investors and private corporations from entering this market. **Yield** The investors investing in these securities gain two types of yields: Running yield or current yield: It is the return on investment (in the current year only) from the interest income and it is calculated as the ratio of the interest income to the purchase price of the security expressed as a percentage. YTM or redemption yield: It is calculated as the return on the investment from the discounted cash flows up to redemption. The coupons are fixed and paid out semi-annually to the holder. The coupons offered on these securities were pre-determined by the Central Bank until 1993 and were kept lower than market interest rates in order to minimize the cost of servicing public debt. From April, 1993, the Reserve Bank has begun auctioning the securities competitively and since then the

interest rates have been increasingly set at market determined levels.

Treasury Bills Purpose

Treasury bills (T-

bills) are raised to meet the short-term funds required by the Government of India. As the Government's revenue collections are bunched and expenses are dispersed, these bills enable it to manage the cash position in a better way. T-bills also enable the RBI to perform Open Market Operations (OMO) which indirectly regulate the

money supply in the economy. Investors prefer Treasury bills because of their

high liquidity, assured returns, no default risk, no capital depreciation and eligibility for statutory requirements. Form T-bills are issued either in the form of a promissory note (or scrip) or credited to the investor's

SGL account. For every class, a standardized format is used. Size The Treasury bills are issued for a minimum amount of ` 25,000 and in multiples of 25,000 thereof. T-bills are issued at

a discount and are redeemed at par. Primary Market in India In India, till April 1992, T-bills of 182 days maturity were issued along with 91-day T-bills. These have since been phased out in favor of 364-day T-bills. In

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in order to enhance the depth of money market in India, the RBI decided to introduce 14-day and 28-day T-bills, along with 91-day, 182-day, 362-day

T- bills. The RBI in its annual monetary and credit policy for the year 2001, withdrew 14-day and 182-day T-bills from May 14, 2001. From April 6, 2005, 182-day Treasury bills were re-introduced.

At present, the GOI (

Government of India) issues three types of T-bills viz., 91-day, 182-day and 364-day.

These instruments make a very liquid market, especially in the short-term. It is because of their liquidity, they form a significant portion of total turnover in the sovereign paper market.

The exhibit below shows the timelines for auctions of treasury bills by RBI Exhibit 11.3: Treasury Bills Auctions by RBI Type of T-Bills

Day of Auction Day of Payment 14-day Friday Following Saturday 91-

day Friday Following Saturday 182-day Wednesday of non-reporting week Following Thursday 364-day Wednesday of reporting week Following Thursday Note: If the day of payment falls on a holiday, the payment is made on the day after the holiday.

Source: <https://www.rbi.org.in/scripts/PublicationsView.aspx?id=1850>

Activity 11.2 a.

Make a comparison of the US treasury bill market with that of the Indian treasury bill market. Do you think the Bill Market in India is under developed? b. What changes occurred in the Government Securities market in India in the post 1991 economic reforms? 11.7

Financial Institutions A Financial System operates through the financial institutions. The financial institutions though mostly operate as lenders, in certain cases they may also function as the borrowers. For a fast developing country like India, these institutions participate in the economic development by extending credit to not

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only businesses but also for developmental activities. The financial institutions operating in India can be segregated into development banks and investment institutions. 11.7.1 All India Development Banks

The All India Development Banks were established with the main objective of extending medium term and long term financial assistance to agriculture and industrial sector. These institutions are:

48%**MATCHING BLOCK 78/173****W**

Industrial Development Bank of India (IDBI) Industrial Development Bank of India (IDBI) was established in 1964 as a subsidiary of the Reserve Bank of India by an Act of the Parliament

88%**MATCHING BLOCK 79/173****SA**

FMG-302 Indian Financial System and Management ...
(D164737022)

Industrial Development Bank of India (IDBI) Industrial Development Bank of India (IDBI) was

and was made a wholly-owned Government of India undertaking in 1975. It was established with the main objective of serving as an apex financial institution to coordinate the functioning of all other financial institutions.

Its other objectives include:

100%**MATCHING BLOCK 80/173****SA**

Shivani Sharma, final thesis.pdf (D30330450)

planning, promoting and developing industries to fill the gaps in the industrial

structure of the country; providing technical and administrative assistance for the promotion or expansion of industry; and

undertaking market and investment research surveys in connection with the development of the industry and to provide finance keeping in view the national priorities, irrespective of the financial attractiveness of projects. IDBI finances industries directly and also supports State Financial Corporations and State Industrial Development Corporations by providing refinance and through the bill rediscounting scheme. IDBI was transformed from financial institution to

a commercial bank in the year 2004.

73%**MATCHING BLOCK 81/173****SA**

FMG-302 Indian Financial System and Management ...
(D164737022)

Industrial Finance Corporation of India (IFCI) Industrial Finance Corporation of India (IFCI) was the first financial institution

76%**MATCHING BLOCK 82/173****SA**

Shivani Sharma, final thesis.pdf (D30330450)

Industrial Finance Corporation of India (IFCI) was the first financial institution to be

established in India in 1948 by an Act of the Parliament with the objective of providing medium and long-term finance to industrial concerns eligible for financing under the Act.

The sectors for which the IFCI provides finance extend through the industrial spectrum of the country. The Export-Import Bank of India (EXIM Bank) The EXIM Bank was set up in 1982 to coordinate the activities of the various institutions engaged in trade finance. It helps Indian exporters in extending credit to their overseas customers by providing long-term finance to them. It also provides assistance to banks in extending credit for exports and export-linked imports. Furthermore, it provides advisory services and information to exporters.

NABARD National Bank for Agriculture and Rural Development (NABARD) was constituted in 1982 in accordance with the recommendations of the committee

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100%

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FMG-302 Indian Financial System and Management ...
(D164737022)

to Review the arrangements for Institutional Credit for Agriculture and Rural

100%

MATCHING BLOCK 84/173

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to Review the arrangements for Institutional Credit for Agriculture and Rural Development (CRAFICARD).

NABARD came into existence in July, 1982 through the transfer of agriculture

71%

MATCHING BLOCK 85/173

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credit functions of RBI and the refinance functions of Agriculture Refinance and Development Corporation.

The functions performed by
the

NABARD can be broadly grouped into three categories – Finance, Developmental and Supervisory. It extends both direct and indirect financial assistance to rural areas. As part of its development functions, it is the apex authority

100%

MATCHING BLOCK 86/173

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for regulating and supervising the functions of co-operative banks and

100%

MATCHING BLOCK 87/173

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003_Banking and Indian financial _16-7-13.pdf (D142522847)

for regulating and supervising the functions of co-operative banks and

regional rural banks. Section 35(6) of the Banking Regulation Act, 1949, empowers NABARD

82%

MATCHING BLOCK 90/173

SA

FMG-302 Indian Financial System and Management ...
(D164737022)

to conduct inspection of State Cooperative Banks (StCBs), Central Cooperative Banks (DCCBs) and Regional Rural Banks (RRBs).

85%

MATCHING BLOCK 89/173

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003_Banking and Indian financial _16-7-13.pdf (D142522847)

of State Cooperative Banks (StCBs), Central Cooperative Banks (DCCBs) and Regional Rural Banks (RRBs).

84%

MATCHING BLOCK 88/173

SA

023E2430_Financial Markets and Institutions.pdf (D165201762)

State Cooperative Banks (StCBs), Central Cooperative Banks (DCCBs) and Regional Rural Banks (RRBs).

100%

MATCHING BLOCK 91/173

SA

003_Banking and Indian financial _16-7-13.pdf (D142522847)

In addition, NABARD has also been conducting periodic inspections of state level cooperative institutions such as State Cooperative Agriculture and Rural Development Banks (SCARDBs), Apex Weavers Societies, Marketing Federations etc., on a voluntary basis.

National Housing Bank It was set up in July, 1988 as an apex level housing finance institution as a wholly owned subsidiary of the RBI. It began its operations with the total capital of ₹ 170 crore (₹ 100 crore as share capital, ₹ 50 crore as long-term loan from the RBI, and ₹ 20 crore through the sale of bonds). In September, 1989, its share capital was raised to ₹ 150 crore. During 1989-90, it issued its second series of bonds whose total subscription amounted to ₹ 60 crore. The RBI sanctioned it a long-term loan of ₹ 25 crore in 1989-90. In 1991-92 it received a loan assistance of Yen 2,970 billion from OECF. By 2010-11, its disbursements crossed ₹ 12,000 crore mark. By 2019-20, its total refinance disbursements crossed ₹ 30,000 crore.

The explicit and primary aim of NHB is to promote housing finance institutions at local and regional levels in the private and joint sectors by providing financial and other support. It refines housing loans under its refinance schemes for scheduled commercial and

91%

MATCHING BLOCK 92/173

SA

Chapter 4 IFS MONEY MARKET final.docx (D156861167)

co-operative banks, housing finance companies, apex co-operative housing finance societies,

and so on.

State Financial Corporations (SFCs) At the beginning of the Fifties, the government found that, for achieving rapid industrialization, separate institutions should be set up that cater exclusively to the needs of the small and medium sector. Therefore the SFCs Act was passed by the Parliament in 1951 to enable the state governments to establish SFCs. The basic objective of SFCs was to provide financial assistance to small and medium scale industries and establish industrial estates. The SFCs provide finance in the form of term loans, by underwriting issues of shares and debentures, by subscribing to debentures, and standing guarantee for loans raised from other institutions and from the general public.

Block IV: Financial Management 90

100%

MATCHING BLOCK 93/173

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FMG-302 Indian Financial System and Management ...
(D164737022)

State Industrial Development Corporations (SIDCs) The State Industrial Development Corporations

78%

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State Industrial Development Corporations (SIDCs) The State Industrial Development Corporations have been set up

to facilitate rapid industrial growth in their respective states. In addition to providing finance, the SIDCs identify and sponsor projects in the joint sector with the participation of private entrepreneurs.

100%

MATCHING BLOCK 94/173

W

Small Industries Development Bank of India (SIDBI) The Small Industries Development Bank of India

75%

MATCHING BLOCK 96/173

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FMG-302 Indian Financial System and Management ...
(D164737022)

Small Industries Development Bank of India (SIDBI) The Small Industries Development Bank of India

40%

MATCHING BLOCK 97/173

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mangal . Intoduction to Financial Markets & In ... (D22478819)

Small Industries Development Bank of India was started in April 1990 under an act of Parliament. It is the major financial institution that promotes financing and development of

April 1990 under an act of Parliament. It is the major financial institution that promotes financing and development of Micro, Small and Medium Enterprises (MSME) sector.

It provides financial support by way of - (a) indirect financing through refinancing facility extended to banks and other financial institutions and (b) direct financing in niche areas like risk capital, sustainable finance, receivables financing, service sector financing etc. The Bank also play a promotional and developmental role by supporting enterprise development, skill up-gradation, marketing support, cluster development, technology modernization etc. MUDRA (Micro Units Development and Refinance Agency Limited) It was started in April 2015 as a specialized institution that provides credit at concessional rates of interest to Micro Finance Institutions and Non-Banking Finance Companies, which in turn will provide the financial assistance to MSMEs. The MUDRA banks were initiated under the Pradhana Mantri MUDRA Yojana scheme, which provide financial assistance to small entrepreneurs who do not come under the ambit of commercial banks. With the help of the NSSO survey conducted in 2013, around 5.77 crore target clients have been identified for rendering the financial assistance.

The borrowers who are eligible for this form of finance include small manufacturing units, shopkeepers, fruit and vegetable vendors and artisans. Three types of loans are being offered by the MUDRA banks – Shishu (loans up to ` 50,000); Kishore (loans up to ` 5,00,000) and Tarun (loans up to ` 10,00,000). 11.7.2

Investment Institutions These institutions channelize the savings of the households into productive investments arenas. These are: Life Insurance Corporation of India (LIC) The LIC was established in 1956 by the

amalgamation and nationalization of 245 private insurance companies by an enactment of the Parliament. The main business of the LIC is to provide life insurance and it has almost a monopoly in this business. The LIC Act permits it to invest up to 10 percent of the investible funds in the private sector. It provides finance by participating in a consortium with other institutions and does not undertake independent appraisal of projects.

Unit 11: Financial System – Indian and International Scenario 91

General Insurance Corporation of India (GIC) The GIC was established in 1974 with the nationalization of the general insurance business in the country. It can invest up to 30 percent of the fresh accrual of funds in the private sector. Like the LIC, the GIC also provides finance by participating in consortium based on the appraisal made by the other financial institutions but does not independently provide the finance. Unit Trust of India (UTI) The UTI was founded in 1964 under the Unit Trust of India Act, 1963. Initially 50 percent of the capital of the trust was contributed by the RBI, while the rest was brought in by the State Bank of India and its associates, LIC, GIC, and other financial institutions. In 1974, the holding of the RBI was transferred to the IDBI, making the UTI an associate of the IDBI. The primary objective of the UTI is to mobilize the savings in the country and channel them into productive corporate investments. UTI provides assistance by underwriting shares and debentures, subscription to public and rights issue of shares and debentures, subscription to private placement, and bridge finance. In January, 2003, UTI was split into two parts UTI-I and UTI-II. UTI-I has been given all the assured return schemes and Unit Scheme 64, and it is being administered by the

Central Government. UTI-II is entrusted with the task of managing NAV- based schemes. UTI-II is being managed by State Bank of India, Punjab National Bank, Bank of Baroda and Life Insurance Corporations. Mutual Funds Mutual funds serve the purpose of mobilization of funds from various categories of investors and channeling them into productive investments. Apart from UTI, mutual funds sponsored by various bank subsidiaries, insurance organizations, private sector financial institutions, DFIs and FIs have come up. These mutual funds operate within the framework of SEBI regulations which prescribe the mechanism for setting up of a mutual fund, procedure of registration, its constitution and the duties, functions and the responsibility of the various parties involved. 11.8

100%	MATCHING BLOCK 99/173	SA	FMG-302 Indian Financial System and Management ... (D164737022)
Functions of Reserve Bank of India The Reserve Bank of India			
48%	MATCHING BLOCK 100/173	SA	book fm(1).doc (D144076294)
Reserve Bank of India The Reserve Bank of India is considered as the nerve center of the Indian monetary system. It was established on 1st April, 1935			
91%	MATCHING BLOCK 101/173	SA	Shivani Sharma, final thesis.pdf (D30330450)
It was established on 1st April, 1935 under the Reserve Bank of India Act. It was a private shareholder'			

s institution till 1947. The bank was nationalized in 1948 under the RBI Act, 1948, soon after independence for three main reasons. Firstly, immediately after the Second World War, central banks all over the world were nationalized. Secondly, to control inflation that has prevailed since 1939, and thirdly, to embark upon a program of economic development and growth in the country.

Block IV: Financial Management 92

Since its inception, the RBI's role has been

guiding, monitoring, regulating, promoting and controlling the Indian financial system. The apex bank was given powers to: regulate the issuance of notes, act as banker to the Government, maintain price stability, and maintain a control over the

money supply in the country. It also has been allowed to carry out open market operations. All the powers were given to Reserve Bank, like any other Central bank in the world, to promote economic development.

One of the main functions of the central bank in any country is monetary management, regulation of the quantity of money, and the supply and availability of credit to business and industry. Similarly, the RBI performs the following functions: Currency Issuing Authority The Reserve Bank of India, since its inception, has the sole right or monopoly authority in issuing the currency in the country, other than one rupee coins/notes and subsidiary coins. Although the one rupee coins are issued by the Central Government, RBI puts them into circulation. It issues notes in denominations of rupees two, five, ten, twenty, fifty, one, five hundred and two

thousand. All the notes carry a guarantee by the central government. The Reserve Bank can issue notes against the security of gold coins, gold bullions, foreign securities, rupee coins, Government of India securities and Bills of exchange and promissory notes, as they are eligible for purchase by

the

Reserve Bank. The responsibility of RBI is not only to put currency into circulation or to

80%

MATCHING BLOCK 102/173

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withdraw from it, but also to exchange notes and coins of one denomination

to the other as demanded by public. The issue department of the Reserve Bank monitors all the matters relating to note issuance.

Government Banker The Reserve Bank acts as a banker not only to the central government, but also to all state governments. It plays a key role by offering all banking services to governments by accepting cheques, receiving and collecting payments, transferring funds, etc. The bank also provides Ways and Means Advances (WMA) to both central and state governments for bridging the temporary gaps between receipts and payments with a maturity of 3 months. There are three different types of WMA; normal or clean WMA, without any underlying security; secured WMA, which are granted against Central Government securities; and finally, special WMA, which are issued by RBI at its discretion. The

Reserve Bank charges interest on the ways and means advances at the repo rate. However, if the WMA is outstanding for more than three months, then the interest rate will be one percent higher than the repo rate.

Unit 11: Financial System – Indian and International Scenario 93

The RBI permits the state government to draw overdrafts apart from Ways and Means Advances.

On such overdrafts, the interest rate charged is as follows: a. On overdrafts up to 100 percent of WMA limit – interest is charged at 2% above the repo rate. b. On overdrafts exceeding 100 percent of WMA limit – interest is charged

at 5% above the repo rate. Issue management and administration of public debts constitute major functions of RBI as a banker to the Governments. Banker's Bank The RBI, like all central banks, can be called

a

banker's bank because it has a unique relationship with scheduled commercial and co-operative banks. The Reserve Bank stipulates that commercial banks maintain the reserves in the form of SLR and CRR. The Reserve Bank provides, in a limited way, avenues for banks to obtain liquidity in the normal course of operation. In case of any crisis, RBI can provide the necessary liquidity support to the banks. Hence, the RBI is known as the 'lender of last resort' to commercial banks. The RBI provides credit to the commercial banks and they in turn provide it to their clients, to promote economic growth. As of now, this is limited to export credit where banks can draw refinance from RBI, subject to conditions. The central bank has the vast power to control commercial and co-operative banks with a view to develop a sound banking system in India. In this regard, the following are the powers given to RBI: ? To issue licenses for establishment of new banks and setting up of branches of existing banks. ? To prescribe minimum requirements regarding paid-up capital and reserves, transfer to reserve fund and maintenance of cash reserves and other liquid assets. ? To inspect the working of banks that are established in India and abroad in respect of their organizational set-up, branch expansion, investments and credit portfolio management, credit appraisal, etc. ? To conduct ad hoc investigations into complaints, irregularities and frauds in respect of banks from time to time. ? To control appointment, reappointment, termination of appointed Chairman and Chief Executive officers of the private sector banks. According to Section 21 of RBI Act, the RBI has been given the power of selective credit control. It is empowered to determine the policy in relation to advances to be followed by banks generally, or by any bank in particular. It is also authorized to issue directions to banks as regards the purpose of the advances, the margins to be maintained for secured advances and also prescribe the interest rate.

Block IV: Financial Management 94

The RBI exercises the selective credit control through the following instruments: ? The bank rate. ? Open market operations. ? Variable reserve requirements.

100%

MATCHING BLOCK 103/173

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Bank Rate: It is the rate at which the Reserve Bank

100%

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Bank Rate: It is the rate at which the Reserve Bank

lends for long term to commercial banks or other financial institutions.

Bank rate is no more used as a credit control tool. Instead, the RBI uses the repo rate, reverse repo rate and MSF rate as tools of credit control.

Repo rate: The Reserve Bank also advances short-term loans to commercial banks with collateral. The interest charged on such loans is the repo rate. The repo rates are changed occasionally by RBI to control the money supply in the economy. A decrease in repo rates make the loans to banks cheaper enabling them to borrow more while an increase in repo rate may have the opposite effect. Reverse Repo Rate: It is the short term borrowing rate at which RBI borrows from banks. It is usually used by RBI to contract the money supply in the economy. Marginal Standing Facility (MSF): This is the borrowing facility given to banks by giving government securities as collateral to meet emergency cash shortage situations. The MSF rate is usually higher than the repo rate.

As on March 30, 2021,
these rates are as follows:

95%	MATCHING BLOCK 104/173	W	
Policy Repo Rate : 4.00% Reverse Repo Rate : 3.35% Marginal Standing Facility Rate : 4.25% Bank Rate : 4.25%			
95%	MATCHING BLOCK 106/173	SA	FMG-302 Indian Financial System and Management ... (D164737022)
Policy Repo Rate : 4.00% Reverse Repo Rate : 3.35% Marginal Standing Facility Rate : 4.25% Bank Rate : 4.25%			

Source: www.rbi.org.in

Open Market Operations: The RBI can influence the reserves of commercial banks, i.e., the cash base of commercial banks, by selling and buying the government securities in the open market. If the RBI buys government securities from commercial banks in the market, the cash transfer will be from RBI to banks and hence, there is an increase in cash base of the commercial banks enabling them to expand credit and converse is the effect if it sells. Usually, the success of the open market operations depends on the size of the government securities available, their range and variety. Most importantly, the prices quoted by RBI should be attractive when compared to the market prices.

Unit 11: Financial System – Indian and International Scenario 95

Variable

Reserve Requirements: The central bank regulates the liquidity of the banking system through two complementary methods such as Cash Reserve Ratio (CRR), and Statutory Liquidity Ratio (SLR). CRR: CRR is the average daily balance with RBI, the percentage of CRR will be specified by RBI from time to time on Net Demand and Time Liabilities (NDTL). It is the cash that banks deposit with Reserve Bank as a proportion of their deposits.

With a view to providing flexibility to banks in choosing an optimum strategy of holding reserves depending upon their intra fortnight cash flows, all SCBs are required to maintain minimum CRR balances up to 95 per cent of the average daily required reserves for a reporting fortnight on all days of the fortnight with effect from the fortnight beginning September 21, 2013.

The CRR on March 30, 2021 is 4% of the bank's total NDTL.

SLR: In addition to the cash reserve ratio, the banks are required to maintain specified reserves in the form of government securities, specified bonds and approved securities.

Consequent upon amendment to the Section 24 of the Banking Regulation Act, 1949 through the Banking Regulation (Amendment) Act, 2007 replacing the Regulation (Amendment) Ordinance, 2007, effective January 23, 2007, the Reserve Bank can prescribe the SLR for SCBs in specified assets. The value of such assets of a SCB shall not be less than such percentage not exceeding 40 per cent of its total DTL in India as on the last Friday of the second preceding fortnight as the Reserve Bank may, by notification in the Official Gazette, specify from time to time.

The SLR on March 30, 2021 is 18%.

Exchange Controls One of the key functions of the Reserve Bank is to maintain the stability of the external value of the Indian rupee. The objective of exchange control is to regulate the demand for foreign exchange within the limits set by the available supply. RBI undertakes: ? To manage exchange reserves. ?

88%

MATCHING BLOCK 107/173

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To administer the foreign exchange control. ? To choose the exchange rate system and fix or manage the exchange

75%

MATCHING BLOCK 108/173

SA FMG-302 Indian Financial System and Management ... (D164737022)

exchange reserves. As the central bank is the custodian of the country's foreign exchange reserves, it is vested with the responsibility of managing

71%

MATCHING BLOCK 109/173

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is the custodian of the country's foreign exchange reserves, it is vested with the responsibility of managing the investment and utilization of reserves in foreign exchange. The Reserve Bank manages buying and selling of foreign exchange from and to commercial banks (who are authorized dealers in Indian forex markets). The apex bank also manages the investment of reserves in gold accounts abroad and the shares and securities issued by foreign governments and international banks or financial institutions.

Block IV:

Financial Management 96

Developmental Activities The central bank has to perform not merely the role of controlling credit and currency to maintain the internal and external value of the rupee to ensure price stability in the economy, but also play the role of a promoter of financial institutions in the country. The bank also performs a wide range of promotional functions to support the pace of economic development. The RBI has been undertaking various steps to promote economic growth in general and markets in particular: i. It has promoted specialized institutions such as SIDBI, NABARD to ensure flow of credit. ii. It has provided agencies like DFHI, STCI as a part of its activity to develop markets. iii. It has introduced various schemes to promote a bill culture. Concept of

Inflation Targeting The concept of Inflation Targeting (IT) received considerable significance in the early 1990s. According to this concept, the central bank of a country brings out a target inflation rate for a medium term and communicates the same to the public. The monetary policy is then so designed as to contain the inflation rate within the target mentioned. The concept was pioneered in New Zealand in 1990 and later implemented in UK, Germany and other countries. Bernanke et.al defined inflation targeting as "a framework for monetary policy characterized by the public announcement of official quantitative targets (or target ranges) for the inflation rate over one or more time horizons, and by explicit acknowledgement that low, stable inflation is monetary policy's primary long-run goal." Benefits One of the major benefits that arise from this concept is that inflation targeting allows monetary policy to "focus on domestic considerations and to respond to shocks to the domestic economy", which is not possible under a fixed exchange- rate system. In addition, investor uncertainty is reduced and therefore investors may more easily factor in likely interest rate changes into their investment decisions. Inflation expectations that are better anchored "allow monetary authorities to cut policy interest rates counter cyclically". Transparency is another important benefit of inflation targeting. Central banks in developed countries, which have successfully implemented inflation targeting were found to "maintain regular channels of communication with the public". An explicit numerical inflation target increases a central bank's accountability, and thus it is less likely that the central bank falls prey to the time- inconsistency trap. This accountability is especially significant because even

Unit 11: Financial System – Indian and International Scenario 97
countries with weak institutions can build public support for an independent central bank. Institutional commitment can also insulate the bank from political pressure to undertake an overly expansionary monetary policy. In 2016, RBI came out with an inflation target of 4% for the next five years i.e., up to 2021.

As per a notification on March 31, 2021, the Central Government in consultation with the RBI, retained the inflation target at 4 percent, with an upper tolerance level of 6 percent and a lower tolerance level of 2 percent. This notification will be valid for a five year period from April 1, 2021 to March 31, 2026.

Exhibit 11.4: Captures Inflation Target vis-à-vis Actual Inflation in India and Other Economies (Per cent) Country Inflation Target
Q1:2020 Q2:2020 Q3:2020 Q4:2020 Q1:2021 Advanced Economies Canada 1.0-3.0 1.8 0.0 0.2 0.8 1.1 Euro area 2.0 1.1 0.2 0.0 -0.3 1.0 Japan 2.0 0.5 0.1 0.2 -0.8 -0.5 UK 2.0 1.7 0.6 0.6 0.5 0.6 US 2.0 1.7 0.6 1.2 1.2 1.5 Emerging Market Economies Brazil 3.75+1.5 3.8 2.1 2.6 4.2 4.9 Russia 4.0 2.4 3.1 3.6 4.4 5.5 India 4.0+2.0 6.7 6.2* 6.9 6.4 4.5 China - 5.0 2.7 2.3 0.1 -0.3 South Africa 3.0-6.0 4.4 2.4 3.1 3.2 3.1 Indonesia 3.0+1.0 2.9 2.3 1.4 1.6 1.5 Philippines 3.0+1.0 2.7 2.3 2.5 1.1 4.5 Thailand 1.0+3.0 0.4 -2.7 -0.7 -0.4 -0.5 Turkey 5.0 12.1 11.7 11.8 13.5 15.6 Source: 11.9

Functions

of Commercial Banks Commercial banks are the oldest, biggest, and fastest growing financial intermediaries in India. They are also the most important depositories of public savings and the most important disbursers of finance. Commercial banking in India is a unique system, and exists nowhere else in the world.

In India, the

banking system has been developed on the lines of social control and public ownership. Banks were nationalized in three phases – in 1955, in July 1969 and in April 1980. All the banks, especially the public sector banks were oriented towards balanced regional development through sectoral deployment of credit and regional distribution of branches and regional deposit

Block IV: Financial Management 98

credit ratios. Several schemes have been introduced at regular intervals such as the

Lead Bank Scheme, Differential Rate of Interest Scheme, Credit Authorization Scheme, inventory norms and lending systems prescribed by the authorities, the formulation of the credit plans, and Service Area Approach to attain the social objectives of the banking system. 11.9.1 Banking Activities Commercial banks are organized on a joint stock company system, which can be either branch banking or unit banking or with a large network of branches with corporate office located at one place. The two essential functions of commercial banks are borrowing from the public in the form of deposits which forms the liability of the bank and lending to the various entities who can be individuals, partnership firms and corporate and are assets for the Bank. Banks pay interest on deposits collected and collect interest on the funds advanced. Banks also provide various other services, which are shown in the following Figure 11.2.

Figure 11.2: Classification of Banking Services Source: ICFAI Research Center

Fund Based Services - Deposits Deposits can be classified into Demand deposits and Term deposits. Savings and current account are demand deposits where the customer can deposit and withdraw at any time. Savings bank accounts are meant to promote savings habit amongst the citizens while allowing them to withdraw the amount any time. This deposit carries simple interest paid half yearly. Though RBI has decontrolled the interest paid on these deposits, Banks maintain lowest interest rate in the savings deposit (around 4% to 4.5%) Current accounts are opened by business class (firms, joint stock companies, clubs and societies, etc.) and the transactions in this account are heavy. Banks do not pay any interest in this type of accounts and on the contrary, levy incidental charges such as folio charges, cheque book issue charges, etc. Term deposits are normally not paid on demand and are retained for a specific period by the customer. These deposits are normally retained from 15 days to even 5 years. The interest paid on these deposits is higher and is compounded quarterly/ half-yearly depending on the type of scheme. Premature withdrawal is

Unit 11: Financial System – Indian and International Scenario 99

permitted but with interest loss to the investor. Recurring deposits are also a kind of fixed deposits. The customer deposits the agreed amount at regular intervals (Monthly/quarterly). The investor gets the principal and interest on the date of maturity. Recurring and fixed deposits are classified as term deposits where the customer retains the amount over a specific period. Most of the banks across the globe have now come up with a hybrid form of deposit called flexi deposit where a portion of the deposit will be in the form of term deposit and the balance in the form of demand deposit. The depositor is able to enjoy both the liquidity of savings and current accounts as well as the high returns of fixed deposits. Though the deposits placed with banks carry low interest, they are relatively a safe mode of investment for the customers who are risk averse. Fund Based Services-Advances Advances can be classified into two broad categories, secured and unsecured or clean. Secured advances are against inventory, receivables, financial instruments, real estate, automobiles, consumer durables and documents of title. There is another classification of advances namely term loans and working capital. Some banks classify the advances as retail (individuals) and wholesale (corporate and large business) advances. Term loans are sanctioned for acquisition of fixed assets such as land, building, plant machinery and other fixed assets. The principal repayment will be on monthly/quarterly or half-yearly basis and the interest has to be serviced on monthly basis. Working capital facilities such as cash credit, packing credit, bills purchase/ discount (both inland and foreign) are considered for acquisition of current assets for day-to-day operations by the bank. Interest is charged on daily outstanding balance and debited to the account on the last day of every month, which has to be serviced by the customer in the first week of the succeeding month. Other Services Financial services- Providing various types of financial services has become an important function of the banking industry today. Investment banking, merchant banking, Bancassurance, foreign exchange business, line of credit service, wealth management service and brokering services are a few of the financial services offered by Banks today. Agency services- This includes collection of cheques, dividends, interests, bills of exchange, etc. on behalf of its customers and crediting the amount in their account is one of the most important agency services rendered by the banks. General utility services - This includes undertaking foreign exchange transactions, issuing letters of credit, accept bills on behalf of customers,

Block IV: Financial Management 100

provide safe custody of valuables, underwrite the issue of shares and debentures, accepting IT payments through banks, provide credit information report, help corporate clients to raise funds in foreign market, undertake factoring and leasing finance, issuing credit and debit cards, etc. Pradhan Mantri JandhanYojna (PMJYD) Pradhan Mantri Jan-DhanYojana (PMJDY) is a National Mission for Financial Inclusion to ensure access to financial services, namely, Banking/ Savings & Deposit Accounts, Remittance, Credit, Insurance, Pension in an affordable manner. Account can be opened in any bank branch or Business Correspondent (Bank Mitra) outlet. PMJDY accounts are opened with zero balance. The account holder can have a RuPay card through which he can withdraw 4 times from any ATM/ month. However, if the account-holder wishes to get a cheque book, he/she will have to fulfill the minimum balance criteria. Eligibility Criteria Any individual who holds Indian nationality, including a minor above the age of 10 with the support of his guardian can open this account. An individual who holds a savings account with the bank can transfer it to Jandhan account. Some of the benefits for depositors under PMJDY are 1) Accidental insurance cover up to ` 1.00 lakh, 2) Provide life cover of ` 30,000/- payable on death of the beneficiary, subject to fulfillment of the eligibility criteria. 3) After satisfactory operation of the account for 6 months, an overdraft facility will be permitted. 4) Access to pension, insurance products. 5) Overdraft facility up to ` 5000/- is available for only one account per household.

In September, 2021, 43.47 Crore beneficiaries banked so far ₹144,791.35 Crore Balance in beneficiary accounts

Asset Liability Management (ALM) Banks and financial institutions face various kinds of risks in the course of their business such as credit risk, market risk, operational risk, liquidity risk etc. Thus, there is a need for effective risk management systems in banks and FIs in a structured manner. ALM is the best solution for handling the various types of risks. Asset Liability Management (ALM) focuses on measuring and monitoring the financial risks other than credit risk in a bank. It focuses on mainly liquidity risk apart from interest rate risk, currency risk, forex risk that affects the liquidity in a bank. Banks try to match the assets and liabilities in terms of maturities and

Unit 11: Financial System – Indian and International Scenario 101

interest rate sensitivities through ALM and hence this exercise can be also called Balance sheet management. Asset Classification The Basel II norms for asset classification require banks to categorize their NPAs into: i. Substandard Assets - With effect from March 31, 2005, a substandard asset would be one, which has remained NPA for a period less than or equal to 12 months. Such assets will have well defined credit weaknesses that jeopardize the liquidation of the debt and are characterized by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected. ii. Doubtful Assets - With effect from March 31, 2005, an asset would be classified as doubtful if it has remained in the substandard category for a period of 12 months. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, – on the basis of currently known facts, conditions and values – highly questionable and improbable. iii. Loss Assets - A loss asset is one where loss has been identified by

87%

MATCHING BLOCK 110/173

SA

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the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly.

87%

MATCHING BLOCK 111/173

SA

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the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly.

In other words, such an asset is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value. Provisioning Norms In conformity with the prudential norms, provisions should be made on the non- performing assets as follows: Loss assets - They should be written off. If loss assets are permitted

to remain in the books for any reason, 100 percent of the outstanding should be provided for.

Doubtful assets – i. 100 percent of the extent to which the advance is not covered by the realizable value of the security, to which the bank has a valid recourse. ii. In regard to the secured portion, provision may be made on the following basis, at the rates ranging from 25 percent to 100 percent of the secured portion

depending upon the period for which the asset has remained doubtful:

Period for which the advance has remained in 'doubtful' category Provision requirement (%) Up to one year 25 One to three years 40

More than three years 100

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iii. Substandard assets - A general provision of 15 percent on total outstanding should be made without making any allowance for ECGC guarantee cover and securities available In Banking system, the Assets are loans and advances and Liabilities are deposits. All the liability figures are considered as outflows while the asset figures are considered as inflows. Banks have to classify the Assets and Liabilities into eight maturity buckets (1-14 days; 15-28 days, 29-90 days, 91- 180 days, 181-365 days, 1-3 years and 3-5 years and above 5 years). As per the RBI guidelines, the mismatches (negative gap) in the time buckets of 1-14 days and 15-28 days should not exceed 20 per cent of the cash outflows in the respective time buckets. Banks are required to monitor their cumulative mismatches across all time buckets in their statement by establishing internal prudential limits with the approval of their boards/ management committees. RBI made it mandatory for banks to form ALCO (Asset Liability Committee) as a Committee of the Board of Directors to track, monitor and report ALM. The ALM process rests on three pillar, which are: 1.

85%	MATCHING BLOCK 112/173	SA	FMG-302 Indian Financial System and Management ... (D164737022)
ALM Information System (Management Information System, Information availability, accuracy, adequacy and expediency) 2. ALM Organization (Structure and responsibilities, Level of top management involvement) 3. ALM Process (Risk parameters, Risk identification, Risk measurement, Risk management,			

Risk policies and tolerance levels) The operating staff of ALM

100%	MATCHING BLOCK 113/173	SA	FMG-302 Indian Financial System and Management ... (D164737022)
should be responsible for analyzing, monitoring and reporting the risk profiles to the			

Asset liability committee (ALCO). The ALCO is a decision-making unit, consisting of senior management, including CEO/ ED and is responsible for integrated balance sheet management. Successful implementation of the risk management process would require a strong commitment on the part of the senior management in the FI, to integrate basic operations and strategic decision making with risk management. 11.9.2. Payment Banks and Small Banks RBI as a part of financial inclusion has come out with two new model banks called Payments Banks and Small Banks in the financial year 2015-16. Payment Banks NachiketMor committee recommended the introduction of payment banks based on Vodafone M-Pesa in Kenya as it observed that 68 percent population did not have bank accounts, but had financial inclusion of 70 percent and this was due to M-Pesa. Payment Banks in India are a new type of banks and are expected to reach customers mainly through their mobile phones rather than traditional bank branches. The target segment of payment banks is the

Unit 11: Financial System – Indian and International Scenario 103

Unorganized Sector, Migrant laborers, Farmers, Low-income households and Small businesses. Payments banks will allow poorer citizens who transact only in cash to take their first step into formal banking. This will lead to a cashless economy. Regulations of Payment Banks Payment Banks in India will be licensed as payment banks under Section 22 of the Banking Regulation Act, 1949 and will be registered as public limited company under the Companies Act, 2013. They will be regulated by RBI. Functions of Payment Banks (PB) a. They can accept deposit up to Rs 1 lakh per customer account (current account or savings account), but cannot sanction loans or issue credit cards. b. They can issue debit card, which can be used on ATM network of all banks. c. They can transfer money directly to bank accounts at almost zero cost. d. They can offer third party card acceptance mechanisms like 'Apple Pay'. e. They can distribute financial products like mutual funds and insurance. f. They can provide forex cards to travelers, usable again as a debit or ATM card all over India. g. They can offer forex services at charges lower than banks. h. Payment banks will have to invest 75% of its demand deposits in Government securities (G-sec) and Treasury bills. i. A maximum of 25% demand deposits can be held as fixed deposits with other scheduled commercial banks. Eleven banks were given in principle approval to start the payment bank by RBI, which includes Department of Post, Aditya Birla Nuvo Ltd, Airtel M Commerce Services Ltd, Cholamandalam Distribution Services Ltd, to name a few. India's domestic remittance market is estimated to be about ` 800-900 billion and growing. With money transfers made possible through mobile phones, many people, especially migrant labor could shift to this new platform. Small Banks Small finance banks are a type of niche banks in India to cater to deposits and loans, particularly in small areas and the clientele includes small farmers, MSMEs, and the unorganized sector. These Small banks will take basic banking services (acceptance of deposits and lending) to unserved and underserved sections of the population. There will be no restriction on the area of operations for small banks, unlike local area bank (LAB)

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Objectives of Small Banks The objectives of small banks are: i. To further the financial inclusion ii. To serve the underserved sections of the population iii. To supply credit to

small business units, small and marginal farmers, micro and small industries; and other unorganized sector

entities through high technology General Guidelines The following are the general guidelines for the establishment of small banks: a.

The Small Banks must have a capital of ` 100 crore. b. Non-banking financial companies (NBFC), micro-finance institutions (MFI) and local area banks (LAB) can set up small finance banks. c. The promoters should have 10 years experience in banking and finance. d.

40% of the paid up capital should be brought in by the promoters. e. Joint ventures are not permitted. f. Foreign share holding will be allowed in these banks. g. The banks will not be restricted to any region. h. 75% of its net credits should be in priority sector lending i.

Maximum of 50% of the loans in its portfolio must be in 25 lakh range. Regulatory Guidelines Besides the above mentioned general guidelines, small banks have to adhere to the following regulatory guidelines. a. The small finance

bank shall be registered as a public limited company under the Companies Act, 2013. b.

It will be licensed under Section 22 of the Banking Regulation Act, 1949 and governed by the provisions of the Banking Regulation

Act, 1949, RBI Act 1934, FEMA 1999 and various other acts. c. The small finance banks will be given scheduled bank status once they commence their operations and found suitable as per Section 42 (6) (a) of the Reserve Bank of India Act, 1934. d. Small banks shall be

required to maintain a minimum capital adequacy ratio of 15 per cent of its risk weighted assets (RWA). e. Tier I capital should be at

least 7.5 per cent of RWAs. f. Tier II capital should be limited to a maximum of 100 per cent of total Tier I capital. 10 entities were

given in principle approval by RBI to set up small banks of which 8 are micro finance institutions. Au Financiers (India) Ltd., Jaipur,

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Capital Local Area Bank Ltd., Jalandhar, Disha Microfin Private Ltd., Ahmedabad, Equitas Holdings P Limited, Chennai are some of the institutions, which got the RBI nod to set up small banks. Jalandhar-based Capital Local Area Bank (CLAB) has become India's first small area finance bank (SFB) and started its operations on April 13, 2016.

11.9.3. Demonetization

Removing the status of legal tender for a currency unit is called demonetization. On 9th November Indian Prime minister Shri Narendra Modi announced demonetization of Rs 500 and Rs 1000, which formed 86% of note circulation ceased to be valid. RBI in its updated notification dated 13th December 2016 stated that the legal tender character of the existing bank notes in denominations of ` 500 and ` 1000 issued by the Reserve bank of India until November 8, 2016 (hereinafter referred to as Specified Bank Notes) stands withdrawn. In consequence thereof, these Bank Notes cannot be used for transacting business and/or store of value for future use.

Significance of Demonetization in November, 2016

In his address to the nation the Prime Minister said that the move was aimed to fight black money (Unaccounted money) in the economy, to lower the cash circulation, which was the main reason for corruption and to eliminate fake currency, which was used to fund terror groups. By making the larger denomination notes worthless, individuals and entities with huge sums of black money can be curtailed. The Government's another goal is to promote cash less economy. This can have positive effects on inflation, lowering tax levels and interests thereby promoting growth.

1. It helps the government to track people who are having large sums of unaccounted cash or cash on which no income tax has been paid.
2. Elimination of fake currency notes which are in circulation.
3. Cash used by terrorists through hawala transactions cannot be put into use and thus reduction in the terror activities.
4. Country will slowly migrate to cashless economy and thereby leads to the elimination of black money.
5. People in remote villages who have hitherto not opened bank accounts will now open accounts thereby helping in financial inclusion.
6. Defaulters of various dues to government are clearing the dues with idle cash that they had.
7. Small vendors have started moving to digital platform.

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Financial Sector Reforms

The decision to nationalize 14 commercial banks in July, 1969 was made to prevent unfair competition and concentration of economic power with industrial houses. But unfortunately with the passage of time it was seen that some public sector banks degenerated into monopoly financial houses.

In spite of the vast expansion in the branch network there was a general decline in efficiency and profits.

11.10.1 Privatization of Banks

Recognizing the need to introduce greater competition in the Indian banking sector, which can lead to greater productivity and efficiency, the RBI allowed the entry of new private sector banks into the banking industry. While permitting the new private sector banks, the RBI set out that they should subserve the underlying goals of the financial sector reforms, be financially viable, carry out upgradation of technology in the banking sector, avoid shortcomings such as unfair pre-emption and concentration of economic power, cross holdings with industrial groups, and other such factors that beset the private sector banks prior to nationalization.

Guidelines for Private Banks

Some of the guidelines laid down by the RBI for establishment of new private sector banks are as follows:

- a. Such a bank shall be registered as a public limited company under the Companies Act, 1956.
- b.

The bank will be governed by the provisions of the

Banking Regulation Act, 1949 with regard to its authorized, subscribed and paid-up capital.

c. The shares of the bank should be listed on stock exchanges. d. To avoid concentration of the headquarters of new banks in metropolitan cities and other overbanked areas, while granting a license, preference may be given to those whose headquarters are proposed to be located in a center which does not have the headquarters of any other bank. e. The new bank shall not be allowed to have as a director any person who is a director of any other banking company, or of companies which among themselves are entitled to exercise voting rights in excess of 20 percent

100%

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of the total voting rights of all the shareholders of the banking company.

f. The bank will be governed by the provisions of the RBI Act, 1934, the Banking Regulation Act, 1949 and other relevant statutes, with regard to its management set up, liquidity requirements and the scope of its activities.

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g. Such a bank shall be subject to prudential norms in respect of banking operations, accounting policies and other policies as laid down by the RBI. h. The bank shall have

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to observe priority sector lending targets as applicable to other domestic banks

i. Such

a bank will also have to comply with such directions of the RBI as are applicable to existing banks in the matter of export credit.

j. A new bank shall not be allowed to set up a subsidiary or mutual fund for at least three years after its establishment. k. Branch opening shall be governed by the existing policy that banks are free to open branches at various centers including urban/metropolitan centers without the prior approval of the RBI once they satisfy the capital adequacy and prudential accounting norms.

Such

a bank shall have to lay down its loan policy within the overall policy guidelines of the RBI. While doing so, it shall specifically provide prudential norms covering related party transactions. m. Such a bank shall make full use of modern infrastructural facilities in office equipment, computer and telecommunications in order to provide good customer service. The bank should have a high powered customer grievance cell to handle customer complaints. n. Such other conditions as the RBI may prescribe from time to time. 11.10.2 Insurance

An insurance is a contract by which insurer agrees to pay the insured a compensation for specified damage, loss or injury suffered in exchange for periodic payment called premium. Classification of Insurance Insurance is basically classified into two categories on the basis of services offered and loss that is insured against. The categories are as follows: i. Life Insurance. ii. General Insurance. Life Insurance: The payment of a sum of money on the death of the insured person due to natural causes (such as disease, old age, debility, etc.), or on the expiry of a certain number of years if the insured person is then alive. General Insurance: Insurances other than life insurance fall within the purview of General Insurance. GI covers loss of every other physical or non-physical possession. The loss may be due to fire, theft, accident, etc. The general insurance is further classified into (i) fire insurance (ii) marine insurance, and (iii) miscellaneous insurance.

Since insurance

is an inevitable necessity, the extent to which it needs to be deregulated becomes a crucial issue. As an extension to liberalization, the

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Government appointed Mr. R.N. Malhotra, former Governor of RBI, to submit a report on how to reform the insurance sector.

Insurance Regulatory and Development Authority (IRDA) The committee opined that the insurance regulatory apparatus should be activated even in the existing setup of nationalized insurance sector and recommended the establishment of strong and effective Insurance Regulatory Authority on the lines of SEBI. Insurance Regulatory Authority was initially constituted through a Government resolution, as was done in the case of SEBI.

The Insurance Regulatory and Development Authority Act, 1999 (IRDA) was enacted in the fiftieth year of the Republic of India. The IRDA is

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a body corporate having perpetual succession and a common seal with power to acquire, hold and dispose of property, and to contract.

It will consist of a Chairperson, not more than five whole-time members and not more than four part-time members. The Chairperson and every other whole-time member shall hold office for a term of five years and shall be eligible for reappointment until the age of 65 years in the case of the Chairperson and 62 years in the case of other whole-time members.

The IRDA shall have the duty to regulate, promote

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and ensure orderly growth of the insurance and re-insurance business. The

powers and functions of the Authority shall include – a.

84%**MATCHING BLOCK 117/173****W**

Protection of the interests of the policyholders in matters concerning assigning of policy, nomination by policyholders, insurable interest, settlement of insurance claim, surrender value of policy and other terms and conditions of contract of insurance;

b. Issue

100%**MATCHING BLOCK 118/173****W**

certificate of registration, renew, modify, withdraw, suspend or cancel such registration;

c.

100%**MATCHING BLOCK 119/173****W**

Specifying requisite qualifications, code of conduct and practical training for intermediary or insurance intermediaries and agents;

d.

100%**MATCHING BLOCK 120/173****W**

Specifying the code of conduct for surveyors and loss assessors;

e.

84%**MATCHING BLOCK 121/173****W**

Promoting efficiency in the conduct of insurance business; f. Promoting and regulating professional organizations connected with the insurance and

reinsurance business; g.

82%**MATCHING BLOCK 122/173****W**

Calling for information from, undertaking inspection of, conducting inquiries and investigations, including audit of the insurers, intermediaries, insurance intermediaries and other organizations connected with the insurance business; h. Control and regulation of rates, advantages, terms and conditions that may be offered by insurers in respect of general insurance business not so controlled and regulated by the Tariff Advisory Committee;

i. Regulating investment of funds by insurance companies;

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j.

100%**MATCHING BLOCK 123/173****W**

Adjudication of disputes between insurers and intermediaries or insurance intermediaries;

k. Supervising the functioning of the Tariff Advisory Committee;

and

l.

100%**MATCHING BLOCK 124/173****W**

Specifying the percentage of life insurance business and general insurance business to be undertaken by the insurer in the rural or social sector.

Ever since liberalization began in the early '90s, there has been intense debate over the extent the insurance sector has to be deregulated in India. The IRDA being the sole regulatory and development authority, would be concentrating on healthy development and orderly growth of one insurance industry in India. Its role has become very important in the wake of the entry of private sector in the insurance industry. 11.10.3 Classification of Non-Banking Financial Companies (NBFCs) The various Non-Banking Financial Companies are explained below:

Investment Trusts or Investment Companies Investment trusts are close-ended organizations, unlike UTI, and they have a fixed amount of authorized capital and a stated amount of issued capital. Investment trusts provide useful services through conserving and managing property for those who, for some reasons or other cannot manage their own affairs. Investors of moderate means are provided facilities for diversification of investment, expert advice on lucrative investment channels, and supervision of their investment. From the point of view of the economy, they help to mobilize small savings and direct them to fruitful channels. They also have a stabilizing effect on stock markets. Unlike in other countries, they render manifold functions such as financing, underwriting, promoting and banking. Most of these companies are not independent; they are investment holding companies, formed by the former managing agents, or business houses. As such, they provide finance mainly to such companies as are associated with these business houses.

Nidhis Mutual benefit funds or nidhis, as they are called in India, are joint stock companies operating mainly in South India, particularly in Tamil Nadu.

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The sources of their funds are share capital, deposits from their members, and the public.

The deposits are fixed and recurring. Unlike other NBFCs, nidhis also accept demand deposits to some extent. The loans given by these institutions are mainly for consumption purposes. These loans are usually secured loans, given against the security of tangible assets such as house property, gold, jewelry, or against shares of companies, LIC policies, and so on. The terms on which loans are given are quite moderate.

Their operations are similar to those of unit banks. They are incorporated bodies and are governed by the directives of the RBI.

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Merchant Banks It would help in understanding the nature of merchant banking if we compare it with commercial banking. The MBs offer mainly financial advice and

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services for a fee, while commercial banks accept deposits and

lend money. When MBs do function as commercial banks, they function essentially as wholesale bankers rather than retail bankers. It means that they deal with selective large industrial clients and not with the general public in their fund based activities. The merchant banks are different from securities dealers, traders, and brokers also. They deal mainly in new issues, while the latter deal mainly in existing securities.

50%**MATCHING BLOCK 128/173****SA**

Chapter 4 IFS MONEY MARKET final.docx (D156861167)

Hire Purchase Finance Companies Hire purchase involves a system under which term loans for purchases of goods and services are advanced to be liquidated

in installments through a contractual obligation. The goods whose purchases are thus financed may be consumer goods or producer goods or they may be simply services such as air travel. Hire-purchase credit may be provided by the seller himself or by any financial institution. Hire-purchase credit is available in India for a wide range of products and services. Products like automobiles, sewing machines, radios, refrigerators, TV sets, bicycles, machinery and equipment, other capital goods, industrial sheds; services like educational fees, medical fees and so on are now financed with the help of such credit. However, unlike in other countries, the emphasis in India is on the provision of installment credit for productive goods and services rather than for purely consumer goods.

Lease Finance Companies A lease is a form of financing employed to acquire the use of assets, through which firms can acquire the economic use of assets for a stated period without owning them. Every lease involves two parties: the user of the asset is known as the lessee, and the owner of the asset is known as the lessor. While these companies may undertake other activities like consumer credit, car finance, etc. their predominant activity is leasing. Lease financing organizations in India include many private sector non-bank financial companies

and some private sector manufacturing companies like Infrastructure Leasing and Financial Services Ltd.

Housing Finance Companies Housing finance is provided in the form of mortgage loans i.e. it is provided against the security of immovable property of land and buildings. Basically, housing finance loans are given by the

Housing and Urban Development Corporation (HUDCO), the apex Co-operative Housing Finance Societies

and Housing Boards in different States, Central and State Governments, LIC,

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Commercial banks, GIC and a few private housing finance companies and nidhis. The

Central and State

Governments provide direct loans mainly to their employees. The participation of commercial and urban co-operative banks in direct mortgage loans has been marginal till recently. LIC has been a major supplier of mortgage loans in indirect and direct forms. It has been giving loans to the State Governments, apex Co-operative Housing Finance Societies, HUDCO, and so on. In addition, it has been providing mortgage loans directly to individuals under its various mortgage schemes. National Housing Bank It was set up in July, 1988 as an apex level housing finance institution as a wholly owned subsidiary of the RBI.

The explicit and primary aim of NHB is to promote housing finance institutions at local and regional levels in the private and joint sectors by providing financial and other support. It refinances housing loans under its refinance schemes for scheduled commercial and

91%**MATCHING BLOCK 129/173****SA**

Chapter 4 IFS MONEY MARKET final.docx (D156861167)

co-operative banks, housing finance companies, apex co-operative housing finance societies,

and so on.

Venture Capital Funding Companies The term “venture capital”, suggests taking risk in supplying capital. However, supply of risk capital may not be a prime function in certain cases; the emphasis may be on supporting technocrats in setting up projects or on portfolio management. The term venture capital fund is usually used to denote mutual funds or institutional investors that provide equity finance or risk capital to little known, unregistered, highly risky, young, small private businesses.

Such businesses often are of the category of

technology-oriented and knowledge-intensive businesses or industries, which have long development cycles and which usually do not have access to conventional sources of capital because of the absence of suitable collateral and the presence of high risk. VCFs play an important role in supplying management and marketing expertise to such units.

Exhibit below discusses the issues faced by NBFCs and the measures taken by the government.

Exhibit 11.5:

Issues Faced by NBFCs and the Measures taken by the Government

The crisis in the Non-Banking Financial Companies (NBFC) sector has been in the making for the past couple of years. While a series of default by well rated NBFCs and Housing Finance Companies like ILFS and Dewan Housing eroded trust-worthiness, a series of other events like Franklin Templeton fiasco and to top it all, the outcome of COVID-19 took a heavy toll on the non-bank sector.

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This necessitated urgent measures to provide relief. Consequently, RBI announced a series of measures from the monetary side while the Government of India complemented the same through stimulus measures to this sector through its five tranche ‘Atmanirbhar Bharat’.

Reasons

for Crisis Asset-Liability mismatches: NBFCs depend on commercial banks, money market instruments i.e. Commercial Paper (CP) and Certificate of Deposits (CD) for their funding requirements which are of short-term in nature. But, they lend to MSMEs, real estate and consumer durable companies for long- term. This creates asset-liability mismatches.

Risk aversion: Moreover, there is restriction on lending by Financial Institutions (FIs) to NBFCs, post IL&FS crisis causing liquidity crunch. Trust in NBFC balance sheets have eroded and even better rated ones find it difficult to raise funds. This will get worse due to COVID-19 when real estate and consumer companies find it hard to repay NBFCs. In short, NBFCs face crisis from two fronts: 1)

Asset-liability mismatches which are already inherent. 2) NBFCs not being able to recover money lent to real estate, consumer durable companies etc. due to the COVID-19 crisis and consequential moratorium. Stimulus package—NBFCs/ HFCs (Housing Finance Companies) & MFIs (Micro Finance Institutions) To provide relief to the crisis-hit NBFCs and HFCs, ₹ 75,000 Crore stimulus package was announced as part of the five tranches. This package has 2 parts: 1. Special liquidity support of ₹ 30,000 Crore - Under

the special liquidity scheme, a special purpose vehicle (SPV) will be created that will invest through both primary market (direct investment when NBFCs issue bonds) and secondary market transactions (purchase of bonds from others who have already bought them) in investment grade bonds issued by NBFCs/HFCs/and MFIs. 2.

Partial Credit Guarantee of ₹ 45,000 Crore -

As the title shows, this scheme does not provide full guarantee for losses suffered on account of investment in NBFC securities. 3.

Together with the special liquidity support, NBFCs/HFCs and MFIs will now receive liquidity support worth ₹ 75,000 Crore under the two schemes.

Source: <https://icfaibytes.in/2020/06/17/nbfc-crisis-and-the-measures-announced-through-atmanirbhar-bharat/>

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Structure of Financial System – International Scenario The international financial system comprises the worldwide framework of financial agreements and financial institutions. It contains both formal and informal economic entities. It facilitates international flows of financial capital for purposes of investment and trade financing. International financial system is the interplay of financial companies, regulators and institutions operating on a supranational level. The global financial system can be broadly divided into two entities. 1. Regulated entities (international banks and insurance companies) 2. Regulators (European Central Bank or the International Monetary Fund) 3. Non-regulated bodies (shadow banking system) which covers hedge funds and private equity 4. Bank sponsored entities such as off-balance-sheet vehicles that banks use to invest in the financial markets International financial system is facing turmoil due to various factors such as financial instability, weak macroeconomic policies, volatile private markets, international capital flows, and weak regulation. The policy guidelines by the new dispensation in US have also added to instability and Governments across the world are watching the developments. For strong global economic strength, improvements are needed in both policy making and the structure of the international financial system. 11.12 Evolution of International Monetary System Different exchange rate systems such as the Gold Standard, the Gold-Exchange Standard, Bretton Woods System, Post Bretton Woods System and the European Monetary System were followed in the past. The Gold Standard The gold standard was followed during the nineteenth century (1870-1914). Except US and UK, which adopted this system from 1821 and 1834 respectively, most of the other countries adopted this system by 1870. Under this system, the governments provided unconditional guarantee to convert their paper money or fiat money into gold on demand at a pre-determined rate at any given time. The exchange rate between currencies was determined based on the price of gold prevalent in the countries. This exchange rate was maintained at an equilibrium level due to possible involvement of arbitrage. Due to transportation costs and transaction costs involved in buying and selling gold, the exchange rate fluctuated between bands on either side of the equilibrium exchange rate. These bands were determined based on the size of costs and subsequently, the end points of the range determined by the bands were termed as gold points. From 1870 to 1913, the paper currency and bank deposits grew rapidly and led to growth in the money supply at a rate of 3 to 4 percent.

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Concern over scarcity of gold led to saving the existing gold in central banks and treasuries and ultimately economizing its use in domestic circulation. Consequently, this exchange rate system was eliminated with the outbreak of World War I in 1914. The Gold Exchange Standard During the war (World War I) period many countries, including Britain borrowed heavily from the US to meet the expenses of food and arms. Creditor nations liquidated most of their foreign assets to finance the war and the debtor nations (mainly US) became creditors, on balance. 18 The war came to an end in 1918 but the exchange rates were allowed to float for some more years. In 1925, Britain adopted a modified version of gold standard at the pre-war parity, slowly followed by other countries. The need for additional liquidity was felt in the international markets. As such, under the new system called gold-exchange standard, some countries converted their currencies into the currency of another country on the gold standard instead of gold. Consequently, instead of holding gold reserves, the countries started holding reserves of that currency into which they had converted their currency. The Great Depression of the late 1920s proved fatal to the US and other countries. It led to low earnings, low demand and much lower employment in addition to the already existing unemployment. Unable to meet its financial obligations, Britain abandoned this system in 1931. With this move, the pressure was completely shifted to the dollar, the only currency convertible to gold. This pressure led to suspending the convertibility by US in 1933. As a result, gold-exchange standard system came to an end. Bretton Woods System In 1944, the representatives of 44 countries met in Bretton Woods, New Hampshire, USA and signed an agreement to bring into force a new monetary system called the Bretton Woods System. The main terms of agreement were as follows: ? Two new institutions, namely International Monetary Fund (IMF) and International Bank for Reconstruction and Development (IBRD or World Bank) were established. IMF would be considered more significant and powerful than the World Bank. All the member countries should work according to the guidelines and instructions provided. ? Adjustable peg system (exchange rate system) was established. ? Currencies must be convertible with regard to trade related activities and other current account transactions, in spite of government's regulations on capital flows. ? The countries could change the exchange rate up to 10% of initial rate, within one year of the rates being determined. ? All the member countries must subscribe towards IMF's capital. 18 The United States became, on balance, a creditor nation by the end of World War I, but only for its wartime loans to the Allies. Most of these loans were never repaid .

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Post-Bretton Woods System (The Current System) As most of the countries were following floating exchange rates after the Bretton woods system, the IMF amended its articles accordingly in Jamaica in 1976 and the same became effective from April 1, 1978. According to the amendment, every country could choose its exchange rate system. It could either float or peg its currency. The currency could be pegged to another currency or to a basket of currencies or SDRs. The only constraint laid down by IMF was that the pegging should not be done with gold. At the same time the member countries were not allowed to fix any official price for gold. They were required to follow the principles adopted by IMF in April 1977. These principles aimed to maintain stability in the Forex markets and also prevent the occurrence of any competitive devaluations. Therefore, different countries adopted different exchange rate systems suitable to their economies.

European Monetary System The basis of the European Monetary Union was the American desire to see a united Western Europe after the World War II. This desire started taking shape when the Europeans created the European Coal and Steel Community, with a view to freeing trade in these two sectors. The pricing policies and commercial practices of the member nations of this community were regulated by a supranational agency. In 1957, the Treaty of Rome was signed by Belgium, France, Germany, Italy, Luxembourg and the Netherlands to form the European Economic Community (EEC), whereby they agreed to make Europe a common market. While they agreed to lift restrictions on movements of all factors of production and to harmonize domestic policies (economic, social and other policies which were likely to have an effect on the said integration), the ultimate aim was economic integration. The European countries desired to make their firms more competitive than their American counterparts by exposing them to internal competition and giving them a chance to enjoy economies of scale by enlarging the market for all of them. The EEC achieved the status of a customs union by 1968. In the same year, it adopted a Common Agricultural Policy (CAP), under which uniform prices were set for farm products in the member countries, and levies were imposed on imports from non-member countries to protect the regional industry from lower external prices. An important roadblock in the European unification was the power given under the treaty to all the member countries, by which they could veto any decision taken by other members. This hindrance was removed when the members approved the Single European Act in 1986, making it possible for a lot of proposals to be passed by weighted majority voting. This paved the way for the unification of the markets for capital and labor, which converted the EEC into a common market on January 1, 1993. Meanwhile, a number of

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countries joined EEC. Denmark, Ireland and the United Kingdom joined in 1973. By 1995, Austria, Finland, Greece, Portugal, Spain and Sweden had also joined, thus bringing the membership to 15. The structure of the EEC consists of the European Commission, a Council of Ministers and a European Parliament. The Commission's members are appointed by the member countries' governments and its decisions are subject to the approval of the Council, where, by convention, either the Finance Ministers or the heads of the central bank represent their respective countries. The members of the Parliament are directly elected by the voters of the member countries. In December 1991, the Treaty of Rome was revised drastically and the group was converted into the European Community by extending its realm to the areas of foreign and defense policies. The members also agreed to convert it into a monetary union by 1999.

European Currency Unit The idea of creating a monetarily stable zone started taking shape in 1978, which resulted in the creation of the European Monetary System in 1979. The system was quite similar to the Bretton Woods System, with the exception that instead of the currencies being pegged to the currency of one of the participating nations, a new currency was created for the purpose. It was named the European Currency Unit (ECU) and was defined as a weighted average of the various European currencies. Each member had to fix the value of its currency in terms of the ECU. This had the effect of pegging these currencies with each other. Whenever the exchange rate between two of the member currencies went beyond the permissible limit, both the countries had to intervene in the forex markets. This co-operation between the countries was expected to make the system more effective. Another important feature of this system was that the members could borrow unlimited amounts of other countries' currencies from the European Monetary Cooperation Fund in order to defend their exchange rates. This was expected to ward off any speculative activities against a member currency. The name "Euro" was officially adopted in 1995 for European Currency Unit and introduced to the financial markets around the world in 1999. Physical currency came into circulation in 2002. The Euro has been trading above the dollar since 2002. However, the European sovereign debt crisis in 2009 de-stabilized the currency and for the first time the Euro traded below the USD. The chances of recovery for Euro further diminished with the Greece Crisis and Spain's banking sector debacle. The currency faced yet another road block with Great Britain opting to exit from the EU.

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Brexit Mounting nationalistic fervor among the British population coupled with unemployment and immigration issues with Germany, another dominant EU member forced the British government to seek for a referendum from the people to stay in or pull out of the European Union. The United Kingdom (UK) on 23 June 2016 voted in a referendum on the country's European Union (EU) membership, and 51.9% of voters chose the option of leaving the EU, which is referred to as Brexit. The implication of this exit from EU can be looked at from four different angles. 1. Geo political implication (Resurgence of nationalism), 2. Global economic implication (Global economic turn down and emerging market crisis), 3. Global security implication (More terrorist attacks on Europe due to increase in right wing extremism in EU) 4. European implication (Confidence in the EU's leadership, the continuing Greek debt crisis and migration crisis.) The Issue for Great Britain after Brexit There would be many complex issues that the UK economy may face due to Brexit over the next decade. Many questions are asked in various forums on the implications for UK trade with the rest of the world: What are the costs and benefits of Brexit? How will Brexit affect UK foreign direct investment? What are the possible alternatives open to the UK once it leaves the European Union etc. According to a study made by Global council UK, the overall macroeconomic impact of Brexit is hard to quantify. This is because there are several unknowns and macro models, which do not capture many areas through which Brexit would affect the economy. The majority of published studies find the impact on the UK would be negative and significant. The impact on the rest of the EU would be smaller, although no comprehensive macroeconomic estimate has been published. It also concludes that the impact of Brexit depends on the relationship with the EU that follows. What is most beneficial politically, in terms of policy independence, is also the most damaging economically. This is the Brexit paradox. 11.13 Role of International Financial Institutions In addition to IMF and World Bank, two more institutions, namely International Finance Corporation (IFC) and International Development Association (IDA) were also established.

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International Monetary Fund (IMF) IMF was established to maintain proper working of the international monetary system. One of its main functions is to provide reserve credit to its member countries to meet temporary problems related to BoP-Balance of payments. IMF is managed by an executive board consisting of 24 directors, among whom six directors are appointed by the governments which hold largest quotas. 19 The highest governing body of IMF is Board of Governors which meets annually to make major policy decisions. Christine Lagarde was appointed as managing director of the IMF for a five-year term starting on 5 July 2011. IMF provides finance to its member countries under various schemes such as Buffer Stock Financing, Compensating Financing, Trust Fund, etc. World Bank The World Bank was established to provide medium and long term loans to the member countries in reconstructing their economies in the post-world war II period and at the same time help the developing countries to increase their economic growth. World Bank is structured like a cooperative that

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is owned and operated for the benefit of its 188 member countries.

Starting its first bond issue in 1947, it has raised

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most of its funds on the world's financial markets

and has become one of the most established borrowers.

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The income earned by IBRD over the years has allowed it to fund development activities

of 188 member countries. This is made possible as it borrows at low cost and offers sovereign clients at competitive terms. International Finance Corporation (IFC) International Financial Corporation is the largest global development institution focused on the private sector. It works closely with businesses in the developing countries to help them succeed in ways that promote prosperity for all. IFC provides investment, advice, and asset management. Together, these services give IFC a special advantage in helping the private sector create opportunity. The ability of IFC to attract other institutional investors brings additional benefits, introducing its investors to new sources of capital and better ways of doing business.

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International Development Association (IDA) The International Development Association (IDA) helps the world's poorest countries. Established in 1960, IDA aims to reduce poverty by providing loans (called "credits") and grants for programs that boost economic growth, reduce inequalities, and improve people's living conditions. IDA

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IDA is one of the largest sources of assistance for the world's 77 poorest countries, 39 of which are in 19

Every member country of IMF must contribute to a currency pool (maintained by IMF) in accordance to its quota, which is fixed based on its importance in the world trade.

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Africa. IDA lends money at

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little or no interest and repayments are stretched over 25 to 38 years, including a 5 – 10 year grace period. IDA also provides grants to countries at risk of debt distress. 11.14

International Financial Instruments Several economies embarked on the liberalization and globalization road during 1980s and 1990s. This led to such economies looking out for markets wherein they could issue dollar/foreign currency denominated shares, since they could not issue such securities in their domestic market. Such economies could access the international equity markets with the aid of an intermediate instrument called 'Depository Receipt'. A Depository Receipt (DR) is a negotiable certificate issued by a depository bank, which represents the beneficial interest in shares issued by a company. These shares are deposited with the local 'custodian' appointed by the depository, which issues receipts against the deposit of shares. There are several instruments that can be accessed to raise funds from international markets:

equity, straight debt or hybrid instruments.

The Figure 11.3 presents the classification of international capital markets on the basis of the instruments used and market(s).

Figure 11.3:

The Structure of International Capital Markets

Source: ICFAI Research Center

Equity Instruments

GDRs GDR stands for Global Depository Receipts. A GDR is a negotiable instrument which represents publicly traded local-currency-equity share. GDR is any instrument in the form of a depository receipt or certificate created by the Overseas Depository Bank outside India and issued to non-resident investors against the issue of ordinary shares or foreign currency convertible bonds of the issuing company. Usually, a typical GDR is

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denominated in US dollars, whereas the underlying shares would be denominated in the local currency of the Issuer. GDRs may be – at the request of the investor – converted into equity shares by cancellation of GDRs through the intermediation of the depository and the sale of underlying shares in the domestic market through the local custodian. GDRs, per se, are considered as common equity of the issuing company and are entitled to dividends and voting rights since the date of its issuance. The company effectively transacts with only one entity – the Overseas Depository – for all the transactions. The voting rights of the shares are exercised by the Depository as per the understanding between the issuing company and the GDR holders. ADRs American Depository Receipts (ADR) is a dollar denominated negotiable certificate, it represents a non-US company's publicly traded equity. It was devised in the late 1920s to help Americans invest in overseas securities and to assist non-US companies wishing to have their stock traded in the American Markets. ADRs are divided into three levels based on the regulation and privilege of each company's issue. i. ADR Level-I: It is often the first step for an issuer into the US public equity market. The issuer can enlarge the market for existing shares and thus diversify the investor base.

In this instrument only minimum disclosure is required to the SEC and the issuer need not comply with the US GAAP (Generally Accepted Accounting Principles).

This type of instrument is traded in the US OTC market.

The issuer is not allowed to raise fresh capital or list on any one of the national stock exchanges. ii. ADR Level-II: Through this level of ADR, the company can enlarge the investor base for existing shares to a greater extent. However, significant disclosures have to be made to the SEC. The company is allowed to list on the American Stock Exchange (AMEX) or New York Stock Exchange (NYSE) which implies that the company must meet the listing requirements of the particular exchange. iii. ADR Level-III: This level of ADR is used for raising fresh capital through public offering in the US Capital Markets. The company has to be registered with the SEC and comply with the listing requirements of AMEX/NYSE while following the US-GAAP.

Debt Instruments Eurobonds

A

Eurobond is an instrument, which is issued in a currency other the currency of the country in which it is issued.

The emergence of Eurobonds can be traced to

Unit 11: Financial System – Indian and International Scenario 121

the 19 th century, when the merchant bankers started dealing in overseas markets. The issue of Eurobonds gained popularity due to the twin advantages associated with these instruments such as the absence of external controls and government restrictions on transfer of funds. Due to varied features, all types of Eurobonds are suitable to any class of issuer or investor. The features of these bonds, which make them unique and flexible, are: a. There is no tax withholding of any kind on interest payments b. Eurobonds are issued in the form of bearer bonds and the interest coupon is attached to the issue.

c. They are listed on one or more stock exchanges but issues are generally traded in the over-the-counter market. A Eurobond is typically issued

in a currency other

the currency of the country in which it is issued.

It resembles

any other Euro instrument and hence through international syndication and underwriting, the bonds can be sold anywhere without any geographical limitations. Eurobonds are listed on most of

the world's stock exchanges, such as the Luxembourg Stock Exchange. a. Fixed-rate Bonds/Straight Debt Bonds:

These bonds come with fixed interest

and are usually redeemed

at face value. The bonds issued in the Euro-market referred to as Euro-bonds, have interest rates fixed with reference to the creditworthiness of the issuer. The interest rate on dollar denominated bonds are set at a margin over the US treasury yields.

These bonds are redeemed by a

bullet payment, i.e. the repayment of debt is done in one lump sum payment at the culmination of the maturity period, and has annual servicing. b. Floating Rate Notes (FRNs):

Floating Rate Notes are bonds that are issued for a maturity period of 5-7 years. These bonds have floating interest rates – the interest rates are either pegged to another security or they are re- determined at periodic intervals. Historically, these bonds have been

referred to as notes and not as bonds. The spreads or margin on these notes

is more than 6 months LIBOR for Eurodollar deposits. Foreign Bonds Foreign bonds are usually issued by foreign entities in order to raise medium and long-term finance from domestic money centers in their domestic currencies. The following instruments are part of Foreign Bonds: a. Yankee Bonds: These are

US dollar denominated bonds which are issued by foreign borrowers (usually foreign governments or entities, supra nationals and

highly rated corporate borrowers) in the bond markets of the US.

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b. Samurai Bonds:

These are bonds issued by non-Japanese borrowers in the domestic Japanese markets.

c. Bulldog Bonds: These are sterling denominated foreign bonds, which are raised in the UK domestic securities market. d. Shibosai Bonds: These are the privately placed bonds issued in the Japanese markets.

Check Your Progress – 2 6. Which among the following is not a type of

Government Security? a. Stock Certificates b. Certificate of Deposits c. Promissory Notes d. Bearer Bonds e. Treasury Bills 7.

This level of ADR is used for raising fresh capital through public offering in the US Capital Markets.

a. ADR Level – I b. ADR Level – II c. ADR Level – III d. ADR Level – IV e. ADR Level – V 8. Which of the following is not a function of

payment banks? a. They can accept deposit up to ` 1 lakh per customer account (current account or savings account), but cannot sanction loans and issue credit cards. b. They can issue debit card and credit cards c. They can transfer money directly to bank accounts at almost zero cost d. They can offer third party card acceptance mechanisms like 'Apple Pay'. e. They can distribute financial products like mutual funds and insurance 9. Which of the following is a control function of RBI for funds requirement of state governments? a. Bank rate b. Open market Operations c. Cash reserve ratio d. Statutory liquidity ratio e. Ways and Means advances

Unit 11: Financial System – Indian and International Scenario 123 10.

Identify the international financial institution that was established to provide medium and long term loans to the member countries in reconstructing their economies in the post-world war II period. a. World Bank b. IFC c. IMF d. IDA e. RBI Self-Assessment Questions -

3 a. Masala Bonds were introduced as Indian Rupee denominated foreign bonds. The first masala bonds issue was taken up by International Financial Corporation in 2014. Analyse the impact made by these bonds in the international market. How do they differ from the other foreign bonds. b. Do you think that Britain's exit from the European Union will result in a negative macro- economic impact on the European Union nations? 11.15

Summary ?

The economic development of a country depends on the progress of its various economic units, namely the Corporate Sector, Government Sector and the Household Sector. The role of the financial sector can be broadly classified into the savings function, and credit function. ? The main types of financial markets are: money market, capital market, forex market and credit market. ? The financial markets are further sub-divided into the Primary market, Secondary market, government securities market. ? The financial institutions in India comprise the RBI, the commercial banks, the Development Banks and the Investment Institutions.

Block IV: Financial Management 124 ? Financial Sector reforms were introduced in 1991, resulted in the privatization of banks, changes in Insurance sector with IRDA and the evolution of NBFCs and Payment banks ? The international financial system comprises the worldwide framework of financial agreements and institutions. It contains both formal and informal economic entities. The financial institutions comprise IMF, World Bank, IFC, IDA etc. ? Several new equity (ADR, GDR) and debt instruments (Euro Bonds, Foreign Bonds) evolved on the horizon of the International financial instruments market. 11.16 Glossary

Bank Rate is the rate at which the Reserve Bank lends for long term to commercial banks or other financial institutions.

Bond is an instrument for long-term debt. Bonus shares are shares issued by companies to existing shareholders out of accumulated profits or free reserves. They are issued as fully paid shares and since the shareholders do not pay, they are also referred to as "free shares".

Bonus shares are issued in the ratio of existing shares held.

Bulldog Bonds are sterling denominated foreign bonds, which are raised in the UK domestic securities

market.
 Commercial Paper (CP) is
 an unsecured usance
 money market instrument issued in the form of a promissory note
 at a discount,
 and is transferable by endorsement and delivery and is of fixed maturity.
 Certificate of Deposit (

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CD) is a negotiable promissory note, secure and short term		

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CD) is a negotiable promissory note, secure and short term		

in nature. CDs

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are issued at a discount to the face value, the discount rate		

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are issued at a discount to the face value, the		

being negotiated between the issuer and the investor.
 Capital is a flexible term that generally refers to financial resources available for use. Thus, the market where capital, represented by stocks and bonds, is traded, constitutes the capital market. It is an over-the-counter market without any physical boundaries where the firm raises funds.
 Eurobond is an instrument, which is issued in a currency other the currency of the country in which it is issued.
 Financial Institutions are institutions engaged in financial activities. Examples: insurance companies, commercial banks, leasing companies.
 Fixed-rate Bonds/Straight Debt Bonds are bonds that come with fixed interest and are usually redeemed at face value. Floating Rate Notes are bonds that are issued for a maturity period of 5-7 years. These bonds have floating interest rates.
 Unit 11: Financial System – Indian and International Scenario 125

GDR is a negotiable instrument which represents publicly traded local- currency-equity share.

Money Market is the market for short-term funds.

Money Market Mutual Funds are those mutual funds that invest mostly in money market instruments. Such money market instruments are of very high quality and of very short maturities. Primary

Market is the market in which financial securities are issued.

Public issue is the most popular method of raising capital and involves raising of funds directly from the public.

Private Placement Market (PPM) financing is the direct sale by a public limited company or private limited company, of private as well as public sector, of its securities (shares and debentures) to a limited number of sophisticated investors like LIC, GIC, State Finance Corporations and Pension and Insurance Funds.

Rights issue is the method of raising additional finance from existing members by offering securities (shares and debentures) to them on pro rata basis.

RBI is the central bank of India and is fully owned by the central government.

Samurai Bonds

are bonds issued by non-Japanese borrowers in the domestic Japanese markets.

Secondary Market is the market for trading of outstanding securities.

Shibosai Bonds are the privately placed bonds issued in the Japanese markets.

Stock Exchanges are formal organizations involved in the trading of securities. Such exchanges are tangible entities that conduct auction in listed securities.

Yankee Bonds are US dollar denominated bonds which are issued by foreign borrowers (usually foreign governments or entities, supra nationals and highly rated corporate borrowers) in the bond markets of the US.

Venture capital fund is usually used to denote mutual funds or institutional investors that provide equity finance or risk capital to little known, unregistered, highly risky, young, small private businesses. 11.17

Self-Assessment Test 1.

Elucidate the functions performed by a Financial System. 2. Describe the functions of the Reserve Bank of India. 3. Explain the functions of different financial institutions in India. 4. Trace the evolution of the international monetary system 5. Evaluate the pros and cons of Brexit. 6. What was the objective of RBI in introducing payment banks? Elucidate the functions performed by such banks.

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Answers to Check Your Progress Questions 1. (d) Social function The functions performed by a financial system are savings, liquidity, risk, policy and payment functions. 2. (e) Maturity periods of 1 -15 days and market determined interest rates

The call money loans are of very short-term in nature and the maturity period of these loans varies from 1 to 15 days.

The

interest paid on call loans is known as the call rate.

Unlike in the case of other short-term and long-term rates, the call rate is expected to reflect the day-to-day availability of funds. These rates vary from day-to-day, often from hour to hour. 3. (

c) Commercial Paper (CP) It

is

an unsecured usance

money market instrument issued in the form of a promissory note

at a discount,

and is transferable by endorsement and delivery and is of fixed maturity.

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c) Dematerialization

Dematerialization is a process by which physical certificates of the investor are destroyed and an equivalent number of securities are credited to his account. 5. (

D) Power to amend Companies Act.

To carry out its functions SEBI has been given various powers which were previously vested with the Central government. These include: ? Power to call for periodical returns from Stock Exchanges subject to the fulfillment of certain criteria. ? Power to call upon the Stock Exchange or any member of the exchange to furnish relevant information. ? Power to appoint any person to make inquiries into the affairs of the Stock Exchange. ? Power to amend

byelaws of the

Stock Exchange. ? Power to compel a public company to list its shares in any Stock Exchange. 6. (

b)

Certificate of Deposits All the others are types of government securities. 7. (c)

ADR Level – III ADR Level – III is used for raising capital through public offering in the US Capital markets 8. (

b) They can issue debit cards and credit cards Payment banks can issue only debit cards and not credit cards 9. (e) Ways and Means

advances Ways and means advances are a form of providing funds to government and not a selective credit control measure. 10. (a)

World Bank World bank is an international financial institution that was established to provide medium and long term loans to the member countries in reconstructing their economies in the post-world war II period.

Unit 12 Time Value of Money Structure 12.1 Introduction 12.2 Objectives 12.3 Meaning of Time Value of Money 12.4 Process of Compounding and Discounting 12.5 Future Value of Cash Flows 12.6

Present Value of Single Cash Flows 12.7

Summary 12.8 Glossary 12.9 Self-Assessment Test 12.10 Suggested Readings/Reference Material 12.11 Answers to Check Your

Progress Questions 12.1

Introduction

The

previous unit
discussed
on

Financial System – Indian and International Scenario.

The economic development of a country depends on the progress of its various economic units - the Corporate Sector, the

Government Sector, and the Household Sector. The role of the financial sector in savings function and credit function

was briefly discussed. Basic information with respect to the money market, capital market, forex market, and credit market was deliberated. The unit further discussed details on the Primary market, Secondary market, government securities market, and ADR. GDR and debt instruments in the international markets were discussed in the previous unit.

The time value of money is an important part of financial management. Time value of money is all about compounding and discounting the rupee value. Suppose you can buy 10 mangoes for ₹ 100 today. However, you can buy only 9 mangoes of the same quality for the same amount after one year. You cannot purchase the same quantity or more because the purchasing power of money has declined in the future. This is called time value of money. Over a period of time, the value of ₹ 100 depreciates. This whole idea, when applied to the business world, means investing in the present market in those projects, which would yield higher return in the future market/period or comparing the future yields from the project to the present market. This unit intends to provide an overview of time value of money and applicability of various concepts of time value of money. 12.2

Objectives ? After reading through the unit, the student should be able to: ? Explain the meaning and concept of time value of money ? Describe the process of compounding and discounting

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Apply the concepts of time value of money in computing future value of cash flows ? Apply the concepts of time value of money in computing present value of cash flows. 12.3 Meaning of Time Value of Money To keep pace with the increasing competition, companies have to go in for new ideas implemented through new projects - be it for expansion, diversification or modernization. A project is an activity that involves investing a sum of money now in anticipation of benefits spread over a period of time in the future. How do we determine whether the project is financially viable or not? Our immediate response to this question will be to sum up the benefits accruing over the future period and compare the total value of the benefits with the initial investment. If the aggregate value of the benefits exceeds the initial investment, the project is considered to be financially viable. While this approach prima facie appears to be satisfactory, we must be aware of an important assumption that underlies. We have assumed that irrespective of the time when money is invested or received, the value of money remains the same. Put differently, we have assumed that: value of one rupee now = value of one rupee at the end of year 1 = value of one rupee at the end of year 2 and so on. We know intuitively that this assumption is incorrect because money has time value. How do we define this time value of money and build it into the cash flows of a project? The answer to this question forms the subject matter of this chapter. We intuitively know that 1,000 in hand now is more valuable than 1,000 receivable after a year. In other words, we will not part with 1,000 now in return for a firm assurance that the same sum will be repaid after a year. But we might part with 1,000 now if we are assured that something more than 1,000 will be paid at the end of the first year. This additional compensation required for parting with 1,000 now is called 'interest' or the time value of money.

Normally, interest is expressed in terms of percentage per annum for example, 12 per cent p.a., or 18 per cent

p.a., and so on. Why should Money have Time Value? Here are some important reasons for this phenomenon: Money can be employed productively to generate real returns. For instance, if a sum of 100 invested in raw material and labor results in finished goods worth 105, we can say that the investment of 100 has earned a rate of return of 5 per cent. In an inflationary period, a rupee today has a higher purchasing power than a rupee in the future. Since future is characterized by uncertainty, individuals prefer current consumption to future consumption.

Unit 12: Time Value of Money 131

The manner in which these three determinants combine to determine the rate of interest can be symbolically represented as follows:

Nominal or Market = Real rate of interest or return + Expected rate of inflation + Risk premiums to compensate for uncertainty

There are two methods by which the time value of money can be taken care of – compounding and discounting.

To understand the basic ideas underlying these two methods, let us consider a project which involves an immediate outflow of say 1,000 and the following pattern of inflows: Year 1: 250 Year 2: 500 Year 3: 750 Year 4: 750 The initial outflow and the subsequent inflows can be represented on a time line as given below

in Figure 12.1: Figure 12.1: Time Line of Cash Outflow and Inflows Yr: 0 1 2 3 4 –1000 250 500 750 750 Source: Adapted from

Prasanna Chandra, Financial Management – Theory and Practice, 8

th edition, New Delhi: Tata McGraw-Hill, 2017. 12.4

Process

of Compounding and Discounting Under the method of compounding, we find the Future Values (FV) of all the cash flows at the end of the time horizon at a particular rate of interest.

Therefore, in this case, we will be comparing the future value of the initial outflow of 1,000 as at the end of year 4 with the sum of the future values of the yearly cash inflows at the end of year 4. This process can be schematically represented as

shown in Figure 12.2: Figure 12.2: Process of Compounding 0 1 2 3 4 –1000 250 500 750 750 + FV (750) + FV (500) + FV (250)

compared with FV (1000) Source:

Prasanna Chandra, Financial Management – Theory and Practice, 8

th edition, New Delhi: Tata McGraw-Hill, 2017.

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Under

the method of discounting, we reckon the time value of money now i.e., at time 0 on the time line. So, we will be comparing the initial outflow with the sum of the Present Values (PV) of the future inflows at a given rate of interest.

This process can be diagrammatically represented as

shown in Figure 12.3: Figure 12.3: Process of Discounting 0 1 2 3 4 –1000 250 500 750 750 Compared with the sums of PV (250) + PV (500) + PV (750) + PV (750) Source: Adapted From

Prasanna Chandra, Financial Management – Theory and Practice, 8

th edition, New Delhi: Tata McGraw-Hill, 2017.

How do we compute the future values and the present values? This question is answered in the latter part of the Unit. But before that, we must draw the distinction between the concepts of compound interest and simple interest. We shall illustrate this distinction through the following illustration. Illustration 12.1 If X has a sum of ₹ 1,000 to be invested, and there are two schemes, one offering a rate of interest of 10 per cent, compounded annually, and other offering a simple rate of interest of 10 per cent, which one should he opt for assuming that he will withdraw the amount at the end of (a) one year, (b) two years, and (c) five years? Solution Given the initial investment of ₹ 1,000, the accumulations under the two schemes will be as follows:

End of Year	Compounded Interest Scheme (₹)	Simple Interest Scheme (₹)
1	1100	1100
2	1210	1200
3	1331	1300
4	1464	1400
5	1610	1500

100%

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$1100 + (1000 \times 0.10) = 1210$
 $1210 + (1210 \times 0.10) = 1331$
 $1331 + (1331 \times 0.10) = 1464$
 $1464 + (1464 \times 0.10) = 1610$
 $1610 + (1610 \times 0.10) = 1771$
 $1771 + (1771 \times 0.10) = 1948.10$
 $1948.10 + (1948.10 \times 0.10) = 2142.91$
 $2142.91 + (2142.91 \times 0.10) = 2357.20$
 $2357.20 + (2357.20 \times 0.10) = 2592.92$
 $2592.92 + (2592.92 \times 0.10) = 2852.21$
 $2852.21 + (2852.21 \times 0.10) = 3137.43$
 $3137.43 + (3137.43 \times 0.10) = 3451.17$
 $3451.17 + (3451.17 \times 0.10) = 3796.29$
 $3796.29 + (3796.29 \times 0.10) = 4175.92$
 $4175.92 + (4175.92 \times 0.10) = 4593.51$
 $4593.51 + (4593.51 \times 0.10) = 5052.86$
 $5052.86 + (5052.86 \times 0.10) = 5558.15$
 $5558.15 + (5558.15 \times 0.10) = 6113.96$
 $6113.96 + (6113.96 \times 0.10) = 6725.36$
 $6725.36 + (6725.36 \times 0.10) = 7397.89$
 $7397.89 + (7397.89 \times 0.10) = 8137.68$
 $8137.68 + (8137.68 \times 0.10) = 8951.45$
 $8951.45 + (8951.45 \times 0.10) = 9846.59$
 $9846.59 + (9846.59 \times 0.10) = 10831.25$
 $10831.25 + (10831.25 \times 0.10) = 11914.38$
 $11914.38 + (11914.38 \times 0.10) = 13105.82$
 $13105.82 + (13105.82 \times 0.10) = 14416.40$
 $14416.40 + (14416.40 \times 0.10) = 15858.04$
 $15858.04 + (15858.04 \times 0.10) = 17443.84$
 $17443.84 + (17443.84 \times 0.10) = 19188.22$
 $19188.22 + (19188.22 \times 0.10) = 21107.04$
 $21107.04 + (21107.04 \times 0.10) = 23217.75$
 $23217.75 + (23217.75 \times 0.10) = 25539.52$
 $25539.52 + (25539.52 \times 0.10) = 28093.47$
 $28093.47 + (28093.47 \times 0.10) = 30892.82$
 $30892.82 + (30892.82 \times 0.10) = 33982.10$
 $33982.10 + (33982.10 \times 0.10) = 37480.31$
 $37480.31 + (37480.31 \times 0.10) = 41328.34$
 $41328.34 + (41328.34 \times 0.10) = 45541.18$
 $45541.18 + (45541.18 \times 0.10) = 50145.30$
 $50145.30 + (50145.30 \times 0.10) = 55160.83$
 $55160.83 + (55160.83 \times 0.10) = 60596.91$
 $60596.91 + (60596.91 \times 0.10) = 66456.60$
 $66456.60 + (66456.60 \times 0.10) = 72742.26$
 $72742.26 + (72742.26 \times 0.10) = 79418.49$
 $79418.49 + (79418.49 \times 0.10) = 86500.34$
 $86500.34 + (86500.34 \times 0.10) = 94000.37$
 $94000.37 + (94000.37 \times 0.10) = 102000.41$
 $102000.41 + (102000.41 \times 0.10) = 110600.45$
 $110600.45 + (110600.45 \times 0.10) = 120060.49$
 $120060.49 + (120060.49 \times 0.10) = 130266.54$
 $130266.54 + (130266.54 \times 0.10) = 141293.19$
 $141293.19 + (141293.19 \times 0.10) = 153262.51$
 $153262.51 + (153262.51 \times 0.10) = 166128.76$
 $166128.76 + (166128.76 \times 0.10) = 180001.64$
 $180001.64 + (180001.64 \times 0.10) = 194901.80$
 $194901.80 + (194901.80 \times 0.10) = 211032.08$
 $211032.08 + (211032.08 \times 0.10) = 228435.29$
 $228435.29 + (228435.29 \times 0.10) = 247298.82$
 $247298.82 + (247298.82 \times 0.10) = 267628.70$
 $267628.70 + (267628.70 \times 0.10) = 289591.57$
 $289591.57 + (289591.57 \times 0.10) = 313350.73$
 $313350.73 + (313350.73 \times 0.10) = 338985.80$
 $338985.80 + (338985.80 \times 0.10) = 366684.38$
 $366684.38 + (366684.38 \times 0.10) = 396552.82$
 $396552.82 + (396552.82 \times 0.10) = 428808.10$
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 $463488.91 + (463488.91 \times 0.10) = 500637.80$
 $500637.80 + (500637.80 \times 0.10) = 540201.58$
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 $582221.74 + (582221.74 \times 0.10) = 626703.91$
 $626703.91 + (626703.91 \times 0.10) = 673674.30$
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 $723141.73 + (723141.73 \times 0.10) = 775215.90$
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 $947416.06 + (947416.06 \times 0.10) = 1010358.67$
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 $1076194.54 + (1076194.54 \times 0.10) = 1145014.00$
 $1145014.00 + (1145014.00 \times 0.10) = 1217015.40$
 $1217015.40 + (1217015.40 \times 0.10) = 1292316.94$
 $1292316.94 + (1292316.94 \times 0.10) = 1370948.63$
 $1370948.63 + (1370948.63 \times 0.10) = 1452943.50$
 $1452943.50 + (1452943.50 \times 0.10) = 1538437.85$
 $1538437.85 + (1538437.85 \times 0.10) = 1627581.64$
 $1627581.64 + (1627581.64 \times 0.10) = 1720529.80$
 $1720529.80 + (1720529.80 \times 0.10) = 1817482.78$
 $1817482.78 + (1817482.78 \times 0.10) = 1918639.06$
 $1918639.06 + (1918639.06 \times 0.10) = 2023909.17$
 $2023909.17 + (2023909.17 \times 0.10) = 2133304.09$
 $2133304.09 + (2133304.09 \times 0.10) = 2246834.50$
 $2246834.50 + (2246834.50 \times 0.10) = 2364519.95$
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 $30130810.53 + (30130810.53 \times 0.10) = 30683621.58$
 $30683621.58 + (30683621.58 \times 0.10) = 31242143.54$
 $31242143.54 + (31242143.54 \times 0.10) = 31806377.90$
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 $32952000.76 + (32952000.76 \times 0.10) = 33533392.84$
 $33533392.84 + (33533392.84 \times 0.10) = 34120505.12$
 $34120505.12 + (34120505.12 \times 0.10) = 34713335.63$
 $34713335.63 + (34713335.63 \times 0.10) = 35311886.19$
 $35311886.19 + (35311886.19 \times 0.10) = 35916166.81$
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 $38390687.37 + (38390687.37 \times 0.10) = 39023688.11$
 $39023688.11 + (39023688.11 \times 0.10) = 39662447.92$
 $39662447.92 + (39662447.92 \times 0.10) = 40306968.71$
 $40306968.71 + (40306968.71 \times 0.10) = 40957259.58$
 $40957259.58 + (40957259.58 \times 0.10) = 41613330.54$
 $41613330.54 + (41613330.54 \times 0.10) = 42275181.59$
 $42275181.59 + (42275181.59 \times 0.10) = 42942811.75$
 $42942811.75 + (42942811.75 \times 0.10) = 43616223.03$
 $43616223.03 + (43616223.03 \times 0.10) = 44295425.33$
 $44295425.33 + (44295425.33 \times 0.10) = 44980429.87$
 $44980429.87 + (44980429.87 \times 0.10) = 45671336.86$
 $45671336.86 + (45671336.86 \times 0.10) = 46368147.55$
 $46368147.55 + (46368147.55 \times 0.10) = 47070862.11$
 $47070862.11 + (47070862.11 \times 0.10) = 47779488.72$
 $47779488.72 + (47779488.72 \times 0.10) = 48494027.39$
 $48494027.39 + (48494027.39 \times 0.10) = 49214480.13$
 $49214480.13 + (49214480.13 \times 0.10) = 49940858.14$
 $49940858.14 + (49940858.14 \times 0.10) = 50673162.15$
 $50673162.15 + (50673162.15 \times 0.10) = 51411392.17$
 $51411392.17 + (51411392.17 \times 0.10) = 52155549.19$
 $52155549.19 + (52155549.19 \times 0.10) = 52905634.21$
 $52905634.21 + (52905634.21 \times 0.10) = 53661649.23$
 $53661649.23 + (53661649.23 \times 0.10) = 54423594.26$
 $54423594.26 + (54423594.26 \times 0.10) = 55191479.28$
 $55191479.28 + (55191479.28 \times 0.10) = 55965304.31$
 $55965304.31 + (55965304.31 \times 0.10) = 56745079.34$
 $56745079.34 + (56745079.34 \times 0.10) = 57530804.37$
 $57530804.37 + (57530804.37 \times 0.10) = 58322489.41$
 $58322489.41 + (58322489.41 \times 0.10) = 59120124.45$
 $59120124.45 + (59120124.45 \times 0.10) = 59923719.50$
 $59923719.50 + (59923719.50 \times 0.10) = 60733274.55$
 $60733274.55 + (60733274.55 \times 0.10) = 61548799.60$
 $61548799.60 + (61548799.60 \times 0.10) = 62370284.66$
 $62370284.66 + (62370284.66 \times 0.10) = 63197729.72$
 $63197729.72 + (63197729.72 \times 0.10) = 64031134.79$
 $64031134.79 + (64031134.79 \times 0.10) = 64870499.87$
 $64870499.87 + (64870499.87 \times 0.10) = 65715824.96$
 $65715824.96 + (65715824.96 \times 0.10) = 66567109.06$
 $66567109.06 + (66567109.06 \times 0.10) = 67424352.16$
 $67424352.16 + (67424352.16 \times 0.10) = 68287554.27$
 $68287554.27 + (68287554.27 \times 0.10) = 69156715.30$
 $69156715.30 + (69156715.30 \times 0.10) = 70031836.33$
 $70031836.33 + (70$

Doubling Period A frequent question posed by the investor is, "How long will it take for the amount invested to be doubled for a given rate of interest." This question can be answered by a rule known as 'rule of 72'. Though it is a crude way of calculating this rule says that the period within which the amount will be doubled is obtained by dividing 72 by the rate of interest. For instance, if the given rate of interest is 6 per cent, then doubling period is $72/6 = 12$ yrs. However, an accurate way of calculating doubling period is the 'rule of 69', according to which, doubling period = $0.35 + 69$

Interest rate

Illustration 12.3 The following is the calculation of doubling period for two rates of interest i.e., 6 per cent and 12 per cent. Solution

Rate of Interest (%) Doubling Period 6 $0.35 + 69/6 = 0.35 + 11.5 = 11.85$ yrs. 12 $0.35 + 69/12 = 0.35 + 5.75 = 6.1$ yrs. Growth Rate The compound rate of growth for a given series for a period of time can be calculated by employing the Future Value Interest Factor Table (FVIF). Illustration 12.4 Years 1 2 3 4 5 6 Profits (in lakh) 95 105 140 160 165 170 How is the compound rate of growth for the above series determined? Solution This can be done in two steps: a. The ratio of profits for year 6 to year 1 is to be determined i.e., $170/95 = 1.79$. b. The FVIF k, n table is to be looked at. Look at a value which is close to 1.79 for the row for 5 years. The value close to 1.79 is 1.762 and the interest rate corresponding to this is 12 per cent. Therefore, the compound rate of growth is 12 per cent.

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Increased Frequency of Compounding In the above illustration, the compounding has been done annually. Suppose, we are offered a scheme where compounding is done more frequently.

Illustration 12.5

For example, assume you have deposited ₹ 10,000 in a bank which offers 10 per cent interest per annum compounded semi-annually which means that interest is paid every six months. Particulars Now, amount in the beginning 10,000 Interest @ 10 per cent p.a., for first six months 0.1 10,000 2 ? ? ? ? ? 500 Amount at the end of six months 10,500 Interest for second 6 months 0.1 10,500 2 ? ? ? ? ? 525 Amount at the end of the year 11,025 Instead, if the compounding is done annually, the amount at the end of the year will be ₹ 10,000 $(1 + 0.1) = ₹ 11,000$. This difference of ₹ 25 is because under semi-annual compounding, the interest for first 6 months earns interest in the second 6 months. The generalized formula for these shorter compounding periods is

$FV_n = PV \times (1 + \frac{k}{m})^n$ Where, $FV_n =$

Future value after 'n' years. $PV =$ Cash flow today. $k =$ Nominal interest rate per annum. $m =$ Number of times compounding is done during a year. $n =$ Number of years for which compounding is done. 12.5.2

Effective vs. Nominal Rate of Interest We have seen above that the accumulation under the semi-annual compounding scheme exceeds the accumulation under the annual compounding scheme by ₹ 25. This means that while under annual compounding scheme, the nominal rate of interest is 10 per cent

per annum, under the scheme where compounding is done semi-annually, the principal amount grows at the rate of 10.25 per cent per annum. This 10.25 per cent is called the effective rate of interest which is

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the rate of interest per annum under annual compounding that produces the same effect as that produced by an interest rate of 10 per cent under

semi-annual compounding. The general relationship between the effective and nominal rates of interest is as follows: $r = 1 + \frac{k}{m}$

where, r = Effective rate of interest. k = Nominal rate of interest. m = Frequency of compounding per year. Illustration

12.6 Find out the effective rate of interest, if the nominal rate of interest is 12 per cent and is quarterly compounded. Solution:

Effective rate of interest $r = 1 + \frac{k}{m}$

$1 + \frac{0.12}{4} = 1.03$

$r = 1.03^4 - 1 = 1.126 - 1 = 0.126 = 12.6\%$ p.a. 12.5.3 Future Value of Multiple Cash Flows Suppose, we invest ` 1,000 now (beginning of year 1), ` 2,000 at the beginning of year 2 and ` 3,000 at the beginning of year 3, how much will these flows accumulate to at the end of year 3 at a rate of interest of 12 per cent per annum? This problem can be represented on the time line as

shown in Figure 12.4: Figure 12.4: Compounding Process for Multiple Flows

Year	0	1	2	3
Flow	1000	2000	3000	
Accumulation				FV (3000) + FV (2000) + FV (1000)

Source: Adapted From

Prasanna Chandra, Financial Management – Theory and Practice, 8

th edition, New Delhi: Tata McGraw-Hill, 2017.

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To determine the accumulated sum at the end of year 3, we have to just add the future compounded values of ` 1,000, ` 2,000 and ` 3,000 respectively. $FV = \frac{1000}{(1 + 0.12)^{-3}} + \frac{2000}{(1 + 0.12)^{-2}} + \frac{3000}{(1 + 0.12)^{-1}}$ At $k = 0.12$, the above sum is equal to = ` 1,000 x FVIF $_{12,3}$ + ` 2,000 x FVIF $_{12,2}$ + ` 3,000 x FVIF $_{12,1}$ = ` [1,000 x 1.405 + 2,000 x 1.254 + 3,000 x 1.120] = ` 7,273 Therefore, to determine the accumulation of multiple flows as at the end of a specified time horizon, we have to find out the accumulations of each of these flows using the appropriate FVIF and sum up these accumulations.

This process can get tedious if we have to determine the accumulation of multiple flows over a long period of time, for example, the accumulation of a recurring deposit of ` 100 per month for 60 months at a rate of 1 per cent

per month. In such cases, a short cut method can be employed provided the flows are of equal amounts. This method is discussed in the following section. 12.5.4

Future Value of Annuity

Annuity is the term used to describe a series of periodic flows of equal amounts.

These flows can be either receipts or payments. For example, if you are required to pay ` 200 per annum as life insurance premium for the next 20 years, you can classify this stream of payments as an annuity. If the equal amounts of cash flow occur at the end of each period over the specified time horizon, then this stream of cash flows is defined as a regular annuity or deferred annuity. When cash flows occur at the beginning of each period the annuity is known as an annuity due. The future value of a regular annuity for a period of n years at a rate of interest ' k ' is given by the formula: $FVA_n = A \left[\frac{(1 + k)^n - 1}{k} \right]$

which reduces to $FVA_n = A \left[\frac{(1 + k)^n - 1}{k} \right]$

Where, A = Amount deposited/invested at the end of every year for n years. k = Rate of interest (expressed in decimals). n = Time horizon.

FVA_n = Accumulation at the end of n years. 20

Candidates who would like to know whether there is any shortcut for evaluating $(1 + k)^n$ for values of 'k' not found in the table, are informed that there is no shortcut method except using logarithms or the XY function found in scientific calculators.

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The expression $FVIFA_{k,n}$

is called the Future Value Interest Factor for Annuity (FVIFA, hereafter) and it represents the accumulation of Re.1 invested or paid at the end of every year for a period of n years at the rate of interest 'k'. As in the case of the future value of a single flow, this expression has also been evaluated for different combinations of 'k' and 'n' and tabulated in Table 2 at the end of this book. So, given the annuity payment, we have to just multiply it with the appropriate FVIFA value and determine the accumulation. Illustration 12.7 Under the recurring deposit scheme of the Vijaya Bank, a fixed sum is deposited every month on or before the due date opted for 12 to 120 months, according to the convenience and needs of the investor. The period of deposit, however, should be in multiples of 3 months only. The rate of interest applied is 9 per cent p.a., for periods from 12 to 24 months and 10

per cent

p.a., for periods from 24 to 120 months and is compounded at quarterly intervals. Solution: Based on the above information, the maturity value of a monthly instalment of ₹ 5 for 12 months can be calculated as below: Amount of deposit = ₹ 5 per month Rate of interest = 9

per cent

p.a., compounded quarterly Effective rate of interest per annum = $1 + \frac{0.09}{4} - 1 = 0.0225$ Rate of interest per month = $(1 + 0.0225)^{1/4} - 1 = 0.0056$

Maturity value can be calculated using the formula

$FVA_n = A \times FVIFA_{k,n}$ $FVA_{12} = ₹ 5 \times FVIFA_{0.0056, 12} = ₹ 62.50$ If the payments are made at the beginning of every year, then the value of such an annuity called annuity due is found by modifying the formula for annuity regular as follows:

$FVA_n(\text{due}) = A \times (1 + k) \times FVIFA_{k,n}$

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Now, that we are familiar with the computation of future value, we will get into the mechanics of computation of present value.

Sinking Fund Factor We have the equation $FVA = A \times FVIFA_{k,n}$

$A = \frac{FVA}{FVIFA_{k,n}}$ We can rewrite it as $A = \frac{FVA}{FVIFA_{k,n}}$ The expression $\frac{1 - (1 + k)^{-n}}{k}$

is called the Sinking Fund Factor. It represents the amount that has to be invested at the end of every year for a period of "n" years at the rate of interest "k", in order to accumulate Re.1 at the end of the period.

Check Your Progress - 11.

Money has time value because a. The individuals prefer future consumption to present consumption. b. A rupee today is worth more than a rupee tomorrow in terms of its purchasing power. c. A rupee today cannot be productively deployed to generate real returns tomorrow. d. The nominal returns on investments are always more than inflation thereby ensuring real returns to the investors. e.

The individuals' consumption decision is not dependent on the purchasing power. 2.

Which of the following statements is true? a. Increased frequency of compounding reduces the effective rate of interest. b.

According to Rule of 72, the period within which the amount will be doubled can be obtained by dividing 72 by the interest rate and adding 0.35 to the value arrived at. c. Effective interest rate is always more than or equal to the nominal interest rate. d. An annuity is a lump sum payment. e. A project is financially viable if the present value of the future cash inflows is positive.

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Time value of money considers a. The preference of the individuals for future consumption to present consumption b. Increase in purchasing power of rupee with the passage of time c. The uncertainty of the future d. The productivity of money to earn real returns over time e.

The certainty of returns in future 4. Under a scheme of Valia Bank, deposits can be made for periods ranging from 6 months to 10 years. Every quarter, interest will be added on to the principal. The rate of interest applied is 9 per cent p.a., for periods from 12 to 23 months and 10 per cent p.a., for periods from 24 to 120 months. How much will an amount of ₹ 1,000 deposited today grow to in two years period? a. ₹ 1,200 b. ₹ 1218 c. ₹ 1118 d. ₹ 1100 e. ₹ 1,018 5.

The nominal rate of interest is equal to a. Real Rate + Risk Premium – Inflation b. Real Rate + Risk Premium + Inflation c. Real Rate – Risk Premium + Inflation d. Real Rate – Risk Premium – Inflation e. Real Rate

Activity 12. 1 a. Ravi wants to buy a bike which costs ₹ 2 lakh. He has ₹ 1 lakh invested in fixed deposits on which he is getting an interest of 7.5%. In how many years, will he be able to buy the bike? b. Ram, a private sector employee, decided to deposit ₹ 30,000 per year in Public Provident Fund (PPF) account for 30 years. What will be the accumulated amount in the PPF account at the end of 30 years if the interest rate is 8% per annum?

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c. You have a choice of receiving ₹ 5,000 now or ₹ 20,000 after 10 years. Which would you choose? What does your preference indicate? 12.6

Present Value of Single Cash Flows Discounting as explained earlier is an alternative approach for reckoning the time value of money. Using this approach, we can determine the present value of a future cash flow or a stream of future cash flows. The present value approach is the commonly followed approach for evaluating the financial viability of projects.

Illustration 12.8 If we invest ₹ 1,000 today at 10 per cent

rate of interest for a period of 5 years, we know that we will get ₹ 1,000 × FVIF (10,5) = ₹ 1,000 × 1.611 = ₹ 1,611 at the end of 5 years. The sum of ₹ 1,611 is called the accumulation of ₹ 1,000 for the given values of 'k' and 'n'. Conversely, the sum of ₹ 1,000 invested today to get ₹ 1,611 at the end of 5 years is called the present value of ₹ 1,611 for the given values of 'k' and 'n'. It, therefore, follows that to determine the present value of a future sum we have to divide the future sum by the FVIF value corresponding to the given values of 'k' and 'n' i.e., present value of ₹ 1,611 receivable at the end of 5 years at 10 per cent rate of interest. = ₹ 1,611 FVIF(10,5) = ₹ 1,611 1.611 = ₹ 1,000 In general, the present value (PV) of a sum (FV n) receivable after n years at a rate of interest (k) is given by the expression. $PV = \frac{FV_n}{FVIF(k,n)}$

$PV = \frac{FV_n}{FVIF(k,n)}$

The inverse of FVIF (k,n) is defined as PVIF (k,n) (Present Value Interest Factor for k,n). Therefore, the above equation can be written as $PV = \frac{FV_n}{FVIF(k,n)}$

$PV = \frac{FV_n}{FVIF(k,n)}$

× PVIF (k,n) Therefore, to determine the present value of a future sum, we have to just locate the PVIF factor for the given values of k and n and multiply this factor value with the given sum. Since PVIF (k,n) represents the present value of Re.1 receivable after n years at a rate of interest k, it is obvious that PVIF values cannot be greater than one. The PVIF values for different combinations of k and n are given in Table 3 at the end of this book.

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Illustration 12.9 Karuna Bank has a

term deposit scheme under reinvestment plan. Interest on deposit money earns interest as it is reinvested at quarterly rests. These deposits suit depositors from lower and middle income groups, since the small odd sums invested grow into large amounts over a period of time. Given an interest rate of 12 per cent p.a., on a certificate having a value of ₹ 100 after 1 year, the issue price of the cash certificate can be calculated as below. Solution:

The

effective rate of interest has to be calculated first. $r = 1$

$m k 1 m ? ? ? ? ? ? ? = 14 0.12 14 ? ? ? ? ? ? ? = 12.55\%$ The issue price of the cash certificate is: $PV = \frac{n}{n+k} (1 + FV)^{-r} = \frac{1}{1+0.1255} (1 + 1255) = 88.85$

Present Value of Uneven Multiple Cash Flows Suppose a project involves an initial investment of ₹ 10 lakh and generates net inflows as follows: End of Year 1 ₹ 2 lakh, 2 ₹ 4 lakh, 3 ₹ 6 lakh. What is the present value of the future cash inflows?

To determine it, we have to first define the relevant rate of interest.

The relevant rate of interest as we shall see later, will be the cost of the funds invested. Suppose, we assume that this cost is 12 per cent p.a., then we can determine the present value of the cash flows using the following two-step procedure: Step 1 Evaluate the present value of cash inflow independently. In this case, the present values will be as follows: Year Cash Flow (₹ in lakh) Present Value (₹ in lakh)
 1 2 $2 \times PVIF(12,1) = 2 \times 0.893 = 1.79$
 2 4 $4 \times PVIF(12,2) = 4 \times 0.797 = 3.19$
 3 6 $6 \times PVIF(12,3) = 6 \times 0.712 = 4.27$

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Step 2 Aggregate the present values obtained in Step 1 to determine the present value of the cash flow stream. In this case, the present value of the cash inflows associated with the project will be ₹ $(1.79 + 3.19 + 4.27)$ lakh = ₹ 9.25 lakh. A project is said to be financially viable if

the present value of the cash inflows exceeds the present value of the cash

outflow. In this case, the project is not financially viable because the present value of the net cash inflows (₹ 9.25 lakh) is less than the initial investment of ₹ 10 lakh. The difference of ₹ 0.75 lakh is called the net present value. Like the procedure followed to obtain the future value of multiple cash flows, the procedure adopted to determine the present value of a series of future cash flows can prove to be cumbersome, if the time horizon to be considered is quite long. These calculations can, however, be simplified if the cash flows occurring at the end of the time periods are equal. In other words, if the stream of cash flows can be regarded as a regular annuity or annuity due, then the present value of this annuity can be determined using an expression similar to the FVIFA expression.

12.6.2 Present Value of Annuity The present value of an annuity 'A' receivable at the end of every year for a period of n years at a rate of interest k is equal to

$PVA = \frac{A}{k} [1 - (1+k)^{-n}]$ which reduces to $PVA = \frac{A}{k} [1 - (1+k)^{-n}]$ The expression $\frac{1 - (1+k)^{-n}}{k}$ is called the PVIFA (Present Value Interest Factor Annuity) and it represents the present value of a regular annuity of Re.1 for the given values of k and n.

The values of PVIFA (k,n) for different combinations of 'k' and 'n' are given in Table 4 given at the end of the book. It must be noted that these values can be used in any present value problem only if the following conditions are satisfied: (a) the cash flows are equal; and (b) the cash flows occur at the end of every year. It must also be noted that PVIFA (k,n) is not the inverse of FVIFA (k,n) although PVIF (k,n) is the inverse of FVIF (k,n). The following illustration illustrates the use of PVIFA tables for determining the present value.

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Illustration 12.10 The Swarna Kalash Yojana at rural and semi-urban branches of SBI is a scheme open to all individuals/firms. A lump sum deposit is remitted and the principal is received with interest at the rate of 12 per cent p.a., in 12 or 24 monthly instalments. The interest is compounded at quarterly intervals. Find out the amount of initial deposit to receive a monthly instalment of ₹ 100 for 12 months. Solution: Firstly, the effective rate of interest per annum has to be calculated. $r =$

$$m k 1 1 m \text{ ? ? ? ? ? ? } = 4 0.12 1 1 4 \text{ ? ? ? ? ? ? } = 12.55\%$$

After calculating the effective rate of interest per annum, the effective rate of interest per month has to be calculated which is nothing but $(1.1255)^{1/12} - 1 = 0.00990$ The initial deposit can now be calculated as below:

$$PVA_n = A n n (1 k) 1 k (1 k) \text{ ? ? ? ? ? ? ? ? } = 100 12 12 (1 0.00990) 1 0.00990 (1 0.00990) \text{ ? ? ? ? ? ? ? ? } = 0.1255 100 0.01114 \text{ ? ? ? ? ? } = 100 \times 11.26 = ₹ 1,126.$$

Capital Recovery Factor Manipulating the relationship between PVA_n , A , k & n we get an equation: $A = PVA_n n n k(1 k) (1 k) 1 \text{ ? ? ? ? ? ? ? ? ? ? }$ Where, $n n k(1 k) (1 k) 1 \text{ ? ? ? ? ? ? ? ? ? ? }$

is known as the capital recovery factor. Illustration 12.11 A loan of ₹ 1,00,000 is to be repaid in five equal annual instalments. If the loan carries a rate of interest of 14 per cent p.a., the amount of each instalment can be calculated as below. If R is defined as the equated annual instalment, we are given that $R \times PVIFA (14\%, 5) = ₹ 1,00,000$ Therefore, $R = (14\%, 5)$

$$Rs. 1,00,000 PVIFA = Rs. 1,00,000 3.433 = ₹ 29,129$$

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We have introduced in this example the application of the inverse of the PVIFA factor which is called the capital recovery factor. The application of the capital recovery factor helps in answering questions like: What should be the amount paid annually to liquidate a loan over a specified period at a given rate of interest? How much can be withdrawn periodically for a certain length of time, if a given amount is invested today? 2. In this example, the amount of ₹ 29, 129 represents the sum of the principal and interest components. To get an idea of the break-up of each instalment between the principal and interest components, the loan repayment schedule is given below:

Year	Equated Annual Instalment	Interest Content of (B)	Capital Content of (B)	Loan Outstanding after Payment (A)	(B) (C)	[(D) = (B) - (C)]	(E) () () () ()
0	–	–	–	1,00,000	1	29,129	14,000
1	29,129	14,000	15,129	84,871	2	29,129	11,882
2	29,129	11,882	17,247	67,624	3	29,129	9,467
3	29,129	9,467	19,662	47,962	4	29,129	6,715
4	29,129	6,715	22,414	25,548	5	29,129	3,577
5	29,129	3,577	25,552	–			

The interest content of each instalment is obtained by multiplying interest rate with the loan outstanding at the end of the immediately preceding year. As can be observed from this schedule, the interest component declines over a period of time whereas the capital component increases. The loan outstanding at the end of the penultimate year must be equal to the capital content of the last instalment but in practice there will be a marginal difference on account of rounding-off errors. 3. The equated annual instalment method is usually adopted for fixing the loan repayment schedule in a hire purchase transaction. But the financial institutions in India like IDBI, IFCI and ICICI do not follow this scheme of equal periodic amortization. Instead, they stipulate that the loan must be repaid in equal instalments. According to this scheme, the principal component of each payment remains constant and the total debt-servicing burden (consisting of principal repayment and interest payment) declines over time. 12.6.3 Present Value of Perpetuity An annuity of an infinite duration is known as perpetuity. The present value of such perpetuity can be expressed as follows: $P = A ?$

$$PVIFA k, ? ?$$

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where, $P =$ Present value of a perpetuity $A =$ Constant annual payment $PVIFA (k, ?) =$ Present value interest factor for a perpetuity. $??$ The value of

$$PVIFA k, ?? \text{ is } k 1 k (1 1 t 1 t \text{ ? ? ? ? ? })$$

We can say that PV interest factor of perpetuity is simply one divided by interest rate expressed in decimal form. Hence, PV of perpetuity is simply equal to the constant annual payment divided by the interest rate.

The various concepts of time value of money discussed above have applications in several areas of finance.

Check Your Progress – 2 6. Discounting is used to determine a.

Future Value of cash flows b. Future Value of annuity c. Present Value of cash flows

d. Doubling period e. Growth rate 7. Mahesh deposits ₹ 200,000 in a bank account which pays 10 per cent interest. How much can he withdraw annually for a period of 15 years? a. ₹ 45,000 b. ₹ 25,596 c. ₹ 26,295 d. ₹ 22,965 e. ₹ 40,000 8. The word annuity refers to

a. Regular stream of cash flows b. Uneven cash flows c. A single lump sum amount d. Amount received at the end of a specific period e. The interest on an investment 9. What is the process of calculating future value of money from present value called? a.

Discounting b. Compounding c. Doubling

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d. Capital Recovery Factor e. Present Value of Perpetuity 10. The relationship between annual nominal rate of interest and annual effective rate of interest, if frequency of compounding is greater than 1 is expressed by the equation a. $ER < NR$ b. $ER > NR$ c. $ER = NR$ d. $ER > NR$ e. $ER \geq NR$ Activity 12.2 a. Pipe Line India Limited is the owner of an oil pipeline that is proposed to generate 10 crore of cash income in the next year. The oil pipeline has a long life and the operating costs are negligible. However, the company predicts that the volume of oil shipped will decline over time. Therefore, the cash flows will decrease by 3 per cent every year. The discount rate is 10%. What do you think will be the present value of cash flows, if it is proposed to use the pipeline forever? b. A wants to borrow ₹ 10,80,000 to buy a one bedroom flat. He approaches PNB Housing Finance which is charging 8.5% interest. If the yearly amount of EMI works out to ₹ 1,00,000, what would be the maturity period of A's loan?

c. A graduate from an engineering college had joined one of the top MNCs. Now, he wants to make some contribution to his college. When he expressed his desire to his professors, they suggested he provide scholarship to bright students. The graduate deposited a certain sum at 10% pa and the scholarship amount was ₹ 10,000 which would be paid yearly for an indefinite period. Find the amount the graduate invested initially.

Block IV: Financial Management 148 12.7 Summary ? Inflation, uncertainty and opportunity cost – whatever the reason, money has time value. ? A rupee today is certainly more valuable than a rupee a year from now, hence the difference usually represented by 'interest.' ? Therefore, two cash flows occurring at different points of time are not comparable. Compounding and discounting are two methods used to take care of time value of money. ? Under the method of compounding, the Future Values (FV) of all the cash flows at the end of the time horizon at a particular rate of interest is ascertained. ? Discounting involves determining the present values of all the future cash flows so that they are comparable to the initial outflow. The rate of interest usually employed is the cost of capital of the firm. 12.8 Glossary Annuity is a stream of fixed payments at regular intervals for a fixed period of time. The fixed payment may be at the beginning or at the end of the intervals. In case the payments are at the beginning of the intervals, it is referred to as Annuity Due. Where payments are made at the end of intervals it is known as Regular Annuity.

Capital Recovery Factor is the ratio of a constant annuity to the present value of receiving that annuity for a given period of time. Compounding is

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Summary ? Inflation, uncertainty and opportunity cost – whatever the reason, money has time value. ? A rupee today is certainly more valuable than a rupee a year from now, hence the difference usually represented by 'interest.' ? Therefore, two cash flows occurring at different points of time are not comparable. Compounding and discounting are two methods used to take care of time value of money. ? Under the method of compounding, the Future

Values (FV) of all the cash flows at the end of the time horizon at a particular rate of interest

is ascertained. ? Discounting involves determining the present values of all the future cash flows so that they are comparable to the initial outflow. The rate of interest usually employed is the cost of capital of the firm. 12.8 Glossary Annuity is a stream of fixed payments at regular intervals for a fixed period of time. The fixed payment may be at the beginning or at the end of the intervals. In case the payments are at the beginning of the intervals, it is referred to as Annuity Due. Where payments are made at the end of intervals it is known as Regular Annuity.

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the method of finding the Future Values (FV) of all the cash flows at the end of the time horizon at a particular rate of interest
Discounting is

the method of finding

the Present Values (PV) of the future inflows at a given rate of interest.

Doubling Period is the amount of time required for an amount to double at a specified rate of interest.

Effective Annual Interest Rate is the annual rate of interest by which an investment multiplies when compounding occurs more than once a year. Future Value is the value of money at a specified date in the future that is equal to a specified sum today at a given

interest rate. Inflation is the rate at which the general price level for goods and services rise, and consequently, purchasing power of money starts falling. Interest is the additional sum paid or received on borrowed money or invested money. It is expressed as a percentage of the principal amount. Perpetuity is the annuity of an infinite duration..

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Present Value is the value of a sum of money today, to be received in the future, at a given interest rate. Rule of 72 is a method used to calculate the number of years required to double the money at a given interest rate. The number of years is calculated by dividing 72 with the given interest rate. 12.9

Self-Assessment Test 1.

How are the effective rate of interest and nominal rate of interest related? 2. Why does money have a time value? 3. Explain the concept of doubling period. What are the different methods used to calculate the doubling period? 4. What is the formula for calculating the present value of an annuity due? 5. How can the present value of multiple cash flows be determined? 6. Explain with the help of an example. 12.10

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Answers to Check Your Progress Questions 1. (

b) A rupee today is worth more than a rupee tomorrow in terms of its purchasing power.

Money has time value as

in an inflationary period, a rupee today has a higher purchasing power than a rupee in the future. 2. (

e) A project is financially viable if the present value of the future cash inflows is positive.

The present value approach is the commonly followed approach for evaluating the financial viability of projects.

Under this approach, projects that generate a positive NPV are accepted. 3. (c) The uncertainty of future Time value of money

considers the uncertainty of future.

Since future is characterized by uncertainty, individuals prefer current consumption to future consumption. 4. (

b) 1,218

FV n = 1,000

$8 \times 0.10 \times 1 + ? + ? + ? + ? + ? + ? = 1,000 \times 1.025^8 = 1,218$

$\times 1.2184 = 1,218$ 5. (b) Real Rate + Risk Premium + Inflation

Nominal or market interest rate = Real rate of interest or return + Expected rate of inflation + Risk premiums to compensate for

uncertainty 6. (

c) Present value of cash flows Discounting is used to determine the present value of cash flows. 7. (c) 26,295 The present value of

Rs.1 @ 10% for 15 years is 7.606. Hence, the annual amount will be $200,000/7.606 = 26,295$ 8. (a) Regular stream of cash flows

Annuity is the term used to describe a series of periodic flows of equal amounts.

These flows can be either receipts or payments. 9. (

b) Compounding Under

the method of compounding, we find the Future Values (FV) of all the cash flows at the end of the time horizon at a particular rate of interest.

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a) ER < NR If frequency of compounding is greater than 1 in a year, then the effective rate of interest will be more than the nominal rate of interest.

This is because the accumulation under semi-annual compounding exceeds the accumulation under annual compounding scheme.

Unit 13 Sources of Long-term and Short-

term Finance Structure 13.1 Introduction 13.2 Objectives 13.3 Need for Long-Term Finance 13.4 Important Sources of Long-term Finance 13.5 Other Sources of Long-Term Finance 13.6 Issue of Securities 13.7

Concept of Short-Term finance for Corporates and Government 13.8 Short-Term Financial Instruments 13.9 Working Capital Management 13.10

Summary 13.11 Glossary 13.12 Self – Assessment Test 13.13 Suggested Readings/Reference Material 13.14 Answers to Check Your Progress Questions 13.1

Introduction

In the previous unit

time value of money. The concepts of Compounding and discounting were discussed along with the present value and future value of monies.

The financial needs of an organization can be broadly classified into two heads: Short-term financial needs; and long-term financial needs. Both these needs are financed either by short-term funds or long-term funds.

It is prudent for an organization to meet its long-term fund requirement from long-term sources of finance rather than short-term sources. The long-term sources comprise shares, debentures and other long-term loans. The short-term financial instruments are treasury bills, commercial paper, certificate of deposits and bills of exchange. Short-term financial decisions are covered under working capital management.

Working capital management is concerned with the problems that arise in attempting to manage the current assets, the current liabilities, and the inter-relationship that exists between them.

This unit provides an insight into the nature of long-term finance and short-

term finance and different types of capital that a company can issue. It also talks about procedure for issue of different securities, short-term financial instruments and the concept of working capital management.

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Management 154 13.2

Objectives After reading through the unit, the student should be able to: ? State the

need for long-term finance ? Identify and explain the different sources of long-term finance ?

Analyse the importance of short-term finance ? Explain the various short-term financial instruments ? Analyze the meaning, need for and

the factors affecting composition of working capital ? Discuss the various stages in the operating cycle 13.3

Need for Long-Term Finance Business firms need finance mainly for two purposes – to fund the long-term decisions and for meeting the working capital requirements. The long-term decisions of a firm involve setting up of the firm, expansion, diversification, modernization and other similar capital expenditure decisions. All these decisions involve huge investment, the benefits of which will be seen only in the long-term and are also irreversible in nature. By nature of these projects, long-term sources of funds become the best suited means of financing. One of the most important considerations for an investment and financing decision will be proper asset-liability management. Companies will have to face a severe asset-liability mismatch if the long-term requirements are funded by the short-term sources of funds. Such a mismatch will lead to an interest rate risk thereby enhancing the interest burden of the firm and a liquidity risk with the short-term funds being held up in long-term projects. Let us consider the costs and means of finance of a project.

Example 13.1 Ponni Sugars & Chemicals Ltd., is setting up a new sugar mill in Orissa. The details of cost of the project and the means of financing are given below: Particulars (₹ in lakh) Cost of the Project: 1.

Land and Site Development 102 2. Buildings 543 3. Plant and Machinery 2,959 4. Miscellaneous Fixed Assets 176 5. Fees for Consultants 55 6.

Preliminary and Pre-operative Expenses 445 7. Provision for Contingencies 210 8. Margin Money for Working Capital 60 Total 4,550

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To bear the cost of financing, the company will look for long-term funding avenues such as the following:

Particulars (₹

in lakh) Means of Financing: 1. Equity Capital: – Promoters 208 – Rights to Shareholders 605 2. Partly Convertible Debentures: – Rights Issue 605 – Public Issue 1600 3. Rupee Term Loan from Financial Institution 1,250 4. Internal Accruals 282

Total 4,550 13.4

Important Sources of Long-Term Finance The sources of long-term financing for firms are generally issues of securities (Equity shares, preference shares, debentures and etc.), term loans, internal accruals, suppliers' credit scheme and equipment financing. In addition to these issues, firms have the option of funding their projects by way of deferred credit, unsecured loans, deposits and venture capital financing. Firms can issue three types of capital – equity, preference, and debenture capital. These three types of capital distinguish amongst themselves in the risk, return and ownership pattern. 13.4.1 Equity Capital Equity share-holders are the owners of the business. They enjoy the residual profits of the company after having paid the preference share-holders and other creditors of the company. Their liability is restricted to the amount of share capital they contributed to the company. Equity capital provides the issuing firm the advantage of not having any fixed obligation for dividend payment but offers permanent capital with limited liability for repayment. However, the cost of equity capital is higher than other capital. Firstly, since the equity dividends are not tax-deductible expenses. Secondly, the high costs of issue. In addition to this, since the equity shareholders enjoy voting rights, excess of equity capital in the firms' capital structure will lead to dilution of effective control. 13.4.2 Preference Capital Preference shares have some attributes similar to equity shares and some to debentures. Like in the case of equity share-holders, there is no obligatory payment to the preference share-holders; and the preference dividend is not tax

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deductible (unlike in the case of the debenture holders, wherein interest payment is obligatory). However, similar to the debenture holders, the preference shareholders earn a fixed rate of return for their dividend payment. In addition to this, the preference shareholders have preference over equity share-holders to the post-tax earnings in the form of dividends; and assets in the event of liquidation. Other features of the preference capital include, the call feature, wherein the issuing company has the option to redeem the shares (wholly or partly) prior to the maturity date and at a certain price. Prior to the Companies Act, 1956, companies could issue preference shares with voting rights. However, with the commencement of the Companies Act, 1956, the issue of preference shares with voting rights has been restricted only in the following cases: i. There are arrears in dividends for two or more years in case of cumulative preference shares. ii. Preference dividend is due for a period of two or more consecutive preceding years. iii. In the preceding six years, including the immediately preceding financial year, if the company has not paid the preference dividend for a period of three or more years. Types of Preference Capital Preference shares can be of two types in three categories.

They are: i.

Cumulative or Non-cumulative preference shares ii. Redeemable or Perpetual preference shares iii. Convertible or non-convertible preference shares For cumulative preference shares, the dividends will be paid on a cumulative basis, in case they remain unpaid in any financial year due to insufficient profits. The company will have to pay up all the arrears of preference dividends before declaring any equity dividends. While on the other hand, the non-cumulative shares do not enjoy such right to dividend payment on cumulative basis. Redeemable preference shares will be redeemed after a given maturity period while the perpetual preference share capital will remain with the company forever. 13.4.3 Debenture Capital A debenture is a marketable legal claim whereby the company promises to pay its owner, a specified rate of interest for a defined period of time and to repay the principal at the specific date of maturity. Debentures are usually secured by a charge on the immovable properties of the company.

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The interest of the debenture holders is usually represented by a trustee and this trustee (which is typically a bank or an insurance company or a firm of attorneys) is responsible for ensuring that the borrowing company fulfils the contractual obligations embodied in the contract. If the company issues debentures with a maturity period of more than 18 months, then it has to create a Debenture Redemption Reserve (DRR), which should be at least half of the issue amount before the redemption commences. The company can also attach call and put options. With the call option the company can redeem the debentures at a certain price before the maturity date and similarly the put option allows the debenture holder to surrender the debentures at a certain price before the maturity period. Types of Debentures Debentures can be classified based on the conversion and security. A few types of debentures are discussed below: Non-Convertible Debentures (NCDs) These debentures cannot be converted into equity shares and will be redeemed at the end of the maturity period. Fully Convertible Debentures (FCDs) These debentures will be converted into equity shares after a specified period of time at one stroke or in installments. These debentures may or may not carry interest till the date of conversion. In the case of a fully established company with an established reputation, and good, stable market price, FCD's are very attractive to the investors as their bonds are getting automatically converted to shares which may at the time of conversion be quoted much higher in the market compared to what the debenture holders paid at the time of FCD issue. Partly Convertible Debentures (PCDs) These are debentures, a portion of which will be converted into equity share capital after a specified period, whereas the non-convertible (NCD) portion of the PCD will be redeemed as per the terms of the issue after the maturity period. The non-convertible portion of the PCD will carry interest right up to redemption whereas the interest on the convertible portion will be only up to the date immediately preceding the date of conversion. Secured Premium Notes (SPNs) This is a kind of NCD with an attached warrant that has recently started appearing in the Indian Capital Market. This was first introduced by Tata Steel which issued SPNs aggregating ₹ 346.50 crore to existing share-holders on a rights basis. Each SPN is of ₹ 300 face value. No interest will accrue on the instrument during the first 3 years after allotment. Subsequently, the SPN will be repaid in 4 equal installments of ₹ 75 each from the end of the fourth year

Block IV: Financial Management 158 together with an equal amount of ₹ 75 with each installment. This additional ₹ 75 can be considered either as interest (regular income) or premium on redemption (capital gain) based on the tax planning of the investor. The warrant attached to the SPN gives the holder the right to apply for and get allotment of one equity share for ₹ 100 per share through cash payment. This right has to be exercised between one and one-and-half year after allotment, by which time the SPN will be fully paid-up.

Provides an insight into the recent long term financial instruments introduced. Non-voting Shares: These shares are issued by companies which try to secure the necessary capital but are not willing to lose the management control. They are equal to equity shares in all aspects, except that they do not have voting rights which are otherwise enjoyed by any equity share-holder. Detachable Equity Warrants: These are issued along with Non-Convertible Debentures (NCDs) or other debt or equity instruments.

They are ideal for growth potential firms, as they will prefer equity coupons to Convertible Debentures (CDs). Participating Debentures: These are unsecured debt securities issued by corporates but with the extra rider that they can participate in the profits of a company. Only existing dividend-paying companies can issue such debentures. These instruments specifically appeal to investors who are willing to accept risk for higher returns. Participating Preference Shares:

These are preference shares which have the right to participate in equity dividends. They are issued as semi-equity instruments and is beneficial to the owners as it does not result in any loss of management control. Dividends pay-outs are linked to equity dividend, and they are

also eligible for bonus. These are preferred by investors with an appetite for low risk. Convertible Debentures with Options:

This instrument is

a derivative of the convertible debentures with an embedded option.

It provides

flexibility to the issuer as well as the investor by enabling them to exit from the terms of the issue. The coupon rate is fixed at the time of the issue. Third Party Convertible Debentures:

This is a debt instrument

with a warranty permitting the investor to subscribe to the equity shares of a third party at a specific price

which is lower than

the market price. Interest rate here is lower than pure debt on account of the conversion option. Mortgage-backed Securities: A

synthetic instrument

also referred to

as the Asset-Backed Security (ABS), for securitization of debt. An ABS is backed by pooled assets like mortgages, credit card receivables, etc. Convertible Debentures Redeemable at Premium:

These are convertible debentures that are issued at face value with a "put" option which enables

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investors to sell the bond at a future date to the issuer at a premium. It caters to the same purpose as a convertible debenture, but the risks to investors are lesser. Debt-equity Swaps: This is a swap option that enables a debt security holder to swap it for equity.

Such an option may carry the risk of dilution of

earnings per share in the case of the issuer; the expected capital appreciation may not materialize in the case of the investor. Zero-

coupon Convertible Note: A Zero-Coupon Convertible Note (ZCCN)

can be converted into equity shares. If investors choose to convert, they have to let go of all accrued and unpaid interest. The risk involved is that these Notes are prone to market risks. 13.5

Other Sources of Long-Term Finance Besides equity and debentures, there are other sources of finance too that can be used for long term funding. These sources are discussed as follows:

Term Loans Term loans constitute one of the major sources of debt finance for a long-term project. Term loans are generally repayable in more than one year but less than 10 years. These term loans are offered by the All India Financial Institutions viz., IDBI, ICICI etc. and by the State Level Financial Institutions. The salient features of the term loans are the interest rates, security offered and the restrictive covenants. The interest rate on the term loans will be fixed after the financial institution appraises the project and assesses the credit risk. Generally, there will be a floor rate fixed for different types of industries. The interest and the principal installment payment are obligatory for the company and any defaults, in this regard will attract a penalty. The company will generally be given 1-2 years of moratorium period, and they will be asked to repay the principal in equal semi- annual installments. Term loans, which can be either in rupee or foreign currency, are generally secured through a first mortgage or by way of depositing title deeds of immovable properties or hypothecation of movable properties. In addition to the security, financial institutions also place restrictive covenants while granting the term loan. These depend mostly on the nature of the project and can include placing the nominees of the financial institution on the company's board, refrain from the company undertaking any new project without their prior approval, disallow any further charges on the assets, maintain the debt-equity ratio to a certain level, etc. The major advantage of this source of finance is its post-tax cost, which is lower than the equity/preference capital and there will be no dilution of control. However, the interest and principal payments are obligatory and threaten the solvency of the firm. The restrictive covenants may, to a certain extent, hinder the company's future plans.

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Internal Accruals Financing through internal accruals can be done through the depreciation charges and the retained earnings. While depreciation amount will be used for replacing an old machinery etc., retained earnings on the other hand can be utilized for funding other long-term objectives of the firms. The major advantages the company gets from using this as a source of long-term finance, are its easy availability, elimination of issue expenses and the problem of dilution of control. However, the disadvantage is that there will be limited funds from this source. In addition to this, ploughing back of retained earnings implies foregoing of dividend receipts by the investors which may actually lead to higher opportunity costs for the firm.

Exhibit 13.1 gives

a corporate example of using internal accruals.

Exhibit 13.1: Using Internal Accruals for Acquisition IndiFrid is a listed infrastructure investment trust (InvIT) formed for financing power transmission lines. In May, 2021, it executed an agreement to acquire power transmission line operator Jhajjar Transco Pvt Limited. The deal was for ₹ 310 crore. IndiFrid was to finance the deal with a mix of debt and its internal accruals. This deal is likely to push the AUM (Assets Under Management) of IndiFrid to ₹ 12,300 crore. Source:

<https://www.livemint.com/companies/news/indigrd-invlt-to-buy-jhajjar-kt-transco-for-rs-310-crore-11590777544290.html>Deferred

Credit

The deferred credit facility is offered by the supplier of machinery, whereby the buyer can pay the purchase price in installments spread over a period of time. The interest and the repayment period are negotiated between the supplier and the buyer and there are no uniform norms. Bill Rediscounting Scheme, Supplier's Line of Credit, Seed Capital Assistance and Risk Capital Foundation Schemes offered by financial institutions are examples of deferred credit schemes. Leasing and Hire Purchase The other sources of finance for companies are the leasing and hire purchase of assets. These two types of financing options, which are supplementary to the actual long-term sources, are offered by financial institutions, Non-Banking Finance Companies, Banks and manufacturers of equipment/assets. Leasing is a contractual agreement between the lessor and the lessee, wherein companies (lessee) can enter into a lease deal with the manufacturer of the equipment (lessor) or through some other intermediary. This deal will give the company the right to use the asset till the maturity of the lease deal and can later return the asset or buy it from the manufacturer. During the lease period the company will have to pay lease rentals, which will generally be at negotiated rate and payable every month. Very similar to leasing is hire purchase, except that in hire purchase the ownership will be transferred to the buyer after all the hire purchase installments are paid-up. With the mushrooming of non-banking

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finance companies offering the leasing and hire purchase of equipments, many companies are opting for this route to finance their assets. The cost of such financing generally lies between 20-25%. Venture Capital Venture Capital means many things to many people. It is in fact nearly impossible to come across one single definition of the concept. Jane Koloski Morris, editor of the well-known industry publication, Venture Economics, defines venture capital as "providing seed, start-up and first stage financing" and also "funding the expansion of companies that have already demonstrated their business potential but do not yet have access to the public securities market or to credit oriented institutional funding sources....". Venture capital also provides management/ leveraged buyout financing. Frederick Radler, a successful practitioner of the profession, describes the process as one of investing in risk capital in an enterprise in which the venture investor shares ownership as well as board of directors level management responsibilities with the founding management team. The European Venture Capital Association describes it as risk finance for entrepreneurial growth oriented companies. It is investment for the medium- or long-term seeking to maximize medium-or long-term return for both parties. It is a partnership with the entrepreneur in which the investor can add value to the company because of his knowledge, experience and contact base. Steven James Lee defines it as "an actual or potential equity investments in companies through the purchase of stock, warrants options or convertible securities". Venture capital is a long-term investment discipline that often requires the venture capitalist to wait for five or more years before realizing a significant return on the capital resource. In an attempt to define venture capital as generically as possible for an international study, International Finance Corporation, Washington DC defines VC as equity or equity featured capital seeking investment in new ideas, new companies, new products, new processes or new services that offer the potential of high returns on investment. It may also include, investment in turnaround situations. A narrow definition of venture capital is, therefore, too limiting. In India, where the industry is still nascent, the Securities and Exchange Board of India has laid down those activities that would constitute eligible business activities qualifying for the concessions available to a recognized venture capital fund. Initially, SEBI defined venture capital as an equity support for projects launched by first generation entrepreneurs using commercially untested but sophisticated technologies. However, this definition has been subsequently relaxed and the restrictive features concerning 'technology financing' were dispensed with. Venture capital is now seen as encompassing all kinds of funding of a high risk technology intensive undertaking at any stage of its life.

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It would appear from the foregoing that venture capital investments would have one or more of the following characteristics: i. Equity or equity-featured instrument of investment ii. Young companies that do not have access to public sources of equity or other forms of capital iii. Industry, products or services that hold potential of better than normal or average revenue growth rates iv. Companies with better than normal or average profitability v. Products/services in the early stages of their life cycle vi. Higher than average risk levels

which

do not lend themselves to systematic quantification through conventional techniques and tools vii. Turnaround companies viii. Long-term (more than three years) and active involvement with investee

Exhibit below describes how Tata Motors is trying to reap benefits through private equity financing Exhibit 13.2: The Search

for a Private Equity Partner – The case of Tata Motors

Companies which are in need of equity can raise through private equity (PE). PE is a form of financing in the form equity by high net worth individuals or institutions invest in fast growing companies, stressed assets, in leveraged buyouts of companies, to fill the gap in equity portion or to strengthen the financial statement which have good potential for turn around. The securities of these companies, that accept private equity unlike public Ltd companies are not listed in stock exchange or traded either.

Benefits and Risks

of PE There are several benefits of PE funds to a company such as access to liquidity, no constant pressure from the investors for publishing quarterly earnings and outflow of cash to meet dividend requirements etc.

Lot of patience is needed by the company which seeks PE partnership. The company should understand the motives and intentions of the PE investor. There has to be a trust and mutual clarity amongst the partners.

Yogendra Vasupal, Rupal Yogendra, and Sachit Singhi with \$ 33.5 million funding started home stay network Stayzilla in India in 2014 and very soon turned out to be the largest homestay network in India. However, the concept was way ahead of its time when launched, as people were not ready for such Hi-Fi technology. By 2017 the firm closed its operations as they could not get further funds.

Contd....

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PE in India India experienced a 33 % jump in PE based on YoY basis touching \$ 27.5 billion for the period January to June 2021. One factor for this growth is that many firms have raised funds from both foreign and domestic investors and the deal sizes are substantial. Tata Motors looking for a PE partner Tata Motors in the process of high growth trajectory in the next ten years is on the lookout for partners especially PE investors for its passenger vehicle segment especially for its EV (electric vehicle) segment. The investments is likely to be in new technology. In this process, the company has planned to carve out the Passenger vehicles as a separate segment on standalone basis and necessary approvals have been obtained from the Board and shareholders as per the company officials during October 2020 and not much developments are seen till June 2021.

Source: <https://icfaibytes.in/2021/08/31/>

100%**MATCHING BLOCK 141/173****W**

scouting-for-a-private-equity-partner-the-case- of-tata-motors/

Government Subsidies The industrial development across the country has not been uniform. Due to various reasons some portions of the country remained backward. In order to remove the anomalies arising out of this unbalanced development, Central and State Governments have been taking various steps to promote these backward areas. One such activity is declaring a particular district or taluq as backward and provides various incentives like investment subsidy, sales tax exemption, subsidy in power billing etc., for industrial units set up in these areas. The investment subsidy varies from state to state.

Sales Tax Deferments and Exemptions To attract industries, the state provides incentives, inter alia, in the form of sales tax deferments and sales tax exemptions. Under the sales tax deferment scheme, the payment of sales tax on the sale of finished goods may be deferred for a period ranging from five to twelve years. Essentially, it implies that the project gets an interest-free loan, represented by the quantum of Sales Tax deferment period. Under the sales tax exemption scheme, some states exempt the payment of sales tax applicable on purchase of raw materials, consumables, packing, and processing materials from within the state which are used for manufacturing purposes. The period of exemption ranges from three to nine years depending on the state and the specific location of the project within the state.

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The below given Exhibit 13.3 provides an example of the sources of long term finance for Tata Steel Limited. Exhibit 13.3: Long-term sources of Finance at Tata Steel Limited as at March 31, 2021 and 2020 (` in crores) As at March 31, 2021 As at March 31, 2020 (a) Secured 2,6777.40 2,633.96 (i) Loans from Joint Plant Committee-Steel Development Fund 2,717.41 2,941.15 (ii) Lease Obligations 5,394.81 5,575.11 (b) Unsecured 13,567.60 12,567.07 (i) Non-Convertible Debentures 8,351.39 13,239.78 (ii) Term Loans from Banks/Financial Institutions 21,918.99 25,806.85 27,313.80 31,381.96 Source: Tata Steel Annual Report 2020-21 13.6

Issue of Securities A firm can raise capital from the primary market (both domestic & foreign) by issuing securities in the following ways: ? Public Issue ? Rights Issue ? Private Placement ? Bought Out Deals ? Euro-Issues The apex body regulating the Indian securities market and the companies raising finance from it, is the Securities and Exchange Board of India (SEBI). Since the Capital Issues Control Act, 1947, was repealed in May, 1992, SEBI was given the statutory power to regulate the Securities Market. 13.6.1

Public Issue Companies issue securities

78%**MATCHING BLOCK 142/173****W**

to the public in the primary market and get them listed on the stock

exchanges. These securities are then traded in the secondary market. The major activities involved in making a public issue of securities are as follows: Appointment of the Lead Manager Before making a public issue of securities, the firm should appoint a SEBI registered Category-I Merchant Banker to manage the issue. The lead manager will be responsible for all the pre and the post-issue activities, liaison with the

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other intermediaries, statutory bodies like SEBI, Stock Exchanges and the Registrar of Companies (ROC), and finally ensures that the securities are listed on the stock exchanges. Preparation of the Prospectus The lead manager is responsible for the preparation of the prospectus. The prospectus is a document that disseminates all the information about the company, the promoters, the objectives of the issue and has the contents as specified by the Company Law. The final prospectus has to be forwarded to SEBI and the listing Stock Exchange. Appointment of Intermediaries The other intermediaries who are involved in the public issue of securities are underwriters, registrars, bankers to the issue, brokers and advertising agencies. Apart from these, it also involves promotion of the issue, printing and dispatch of prospectus and application forms, obtaining statutory clearances, filing the initial listing application, final allotment and refund activities. The cost of a public issue ranges between 12-15% of the issue size and can go up to 20% in bad market conditions.

13.6.2 Rights Issue Under Section 81 of the Companies Act, 1956, when a firm issues additional equity capital, it has to first offer such securities to the existing shareholders on a pro rata basis. The rights offer should be kept open for a period of 60 days and should be announced within one month of the closure of the books. The share-holders can also renounce their rights in favor of any other person at market determined rate. The cost of floating of rights issue will be comparatively less than the public issue, since these securities are issued to the existing share-holders, thereby eliminating the marketing costs and other relevant public issue expenses. The rights issue will also be priced lower than the public issue since it will be offered to the existing share-holders.

Ex-rights Value of a Share The value of a

share, after the rights issue, is $\frac{1}{N} \left(\frac{S}{P_0} + 1 \right)$ Where, N = number of existing shares required for one rights share. P₀ = cum-rights price per share. S = subscription price at which rights shares are issued.

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Illustration 13.1 If a company issues one share for every 3 shares held

at a price of ₹ 25 per share, and the existing price is ₹ 30 per share, find the

ex-rights price of the share. Solution The value of a share, after the rights issue =

$\frac{1}{N} \left(\frac{S}{P_0} + 1 \right) = \frac{1}{3} \left(\frac{25}{30} + 1 \right) = ₹ 28.75$

per share. The Theoretical Value of a Right It is a mathematically determined market value of a subscription right after the offering is announced but before the stock goes ex-rights. The formula to find theoretical value of a right is

$\frac{1}{N} \left(\frac{S}{P_0} + 1 \right)$

In the above example, it would be $= \frac{1}{4} (30 - 25) = ₹ 1.25$

13.6.3 Private Placement The Private Placement (PP) method of financing

involves direct selling of securities to a limited number of institutional or high net worth

investors. This avoids the delay involved in going public and also reduces the expenses involved in a public issue. The companies appoint a merchant banker to network with the institutional investors and negotiate the price of the issue. The major advantage of privately placing the securities is: ? Easy access to any company ? Fewer procedural formalities ? Lower issue cost ? Access to funds is faster

13.6.4 Bought-Out-Deals

Buy-out is a process whereby an investor or a group of investors buy-out a significant portion of the equity of an unlisted company with a view to

sell the equity to public within an agreed time-frame. The company places the equity shares, to be offered to the public, with a sponsor. At the right time, the shares will be offloaded to the public through the OTCEI route or by way of a public issue. The bought-out deal route is relatively inexpensive, funds accrue without much delay (in a public issue funds reach the company only after a period of 2-3 months from the date of closure of the subscription list). In addition to this, it affords greater flexibility in terms of the issue and matters relating to

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offloading

with proper negotiations with the sponsor or the Merchant Banker involved. Major advantages of entering into a bought-out deal are: Companies, both existing and new, which do not satisfy conditions laid down by SEBI for premium issues, may issue at a premium through the BOD method. The procedural complexities are reduced considerably and the funds reach the firm upfront. Added to this, there is a cut in the issue costs. An advantage accruing the investor is that the issue price usually reflects the company's intrinsic value. 13.6.5 Euro-Issues The Government has allowed Indian companies to float their stocks in foreign capital markets. The Indian corporates, which face high rates of interest in the domestic markets are now free to tap the global capital markets for meeting resource requirements at less costs and administrative problems. The instruments which the company can issue are, Global Depository Receipts (GDRs), Euro-Convertible Bonds (ECBs), and Foreign Currency Convertible Bonds (FCCBs). These instruments are issued abroad and listed and traded on a foreign stock exchange. Once they are converted into equity, the underlying shares are listed and traded on the domestic exchange.

100%

MATCHING BLOCK 144/173

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mangal . Intoduction to Financial Markets & In ... (D22478819)

Check Your Progress – 1 1. Which of the following is not a

type of issue of securities? a. Public issue b. Rights issue c. Private placement d. Euro issue e. Issue of Treasury bills 2. Which type of long-term finance is defined as "risk finance for entrepreneurial growth-oriented companies"? a. Venture capital b. Internal accruals c. Leasing d. Deferred credit e. Term loans 3. One of the following is not an advantage of private placement. Identify a. Easy access to the company b. Fewer procedural formalities c. Lower issue cost d. Access to funds is limited e. Access to funds is faster

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When a company makes a rights issue, which of the following is true regarding the wealth of the existing share-holders? a. It will increase if he sells his

right

b. It will not be affected, if he allows his rights to expire c. It will increase if he exercises the right d. It will decrease if he allows the right to expire e.

It will increase if he exercises the right and decreases if he allows the right to expire. 5.

Which one of the following is not a source of long-term finance? a. Equity capital b. Preference capital c. Debenture capital d.

Commercial paper e. Term loan Activity 13.1 a.

It

is a process whereby an investor or a group of investors buy-out a significant portion of the equity of an unlisted company with a view to

sell the equity to public within an agreed time-frame. Identify the form of finance described above and state its benefits.

b. Company XYZ, which had concentrated its operations in India only, is now all set to be a global company. So, it is planning to raise additional funds. The company already has 4,50,000 equity shares and is planning to sell 1,50,000 new equity shares. The company would issue shares at a price of ₹ 25 per share, and the existing price is ₹ 30 per share. Calculate the value of right. 13.7

Concept of Short-Term Finance for Corporates and Government Governments borrow long-term funds to invest in public sector institutions of production or to build social infrastructure like educational institutions, hospitals, roads etc. The government on the other hand may borrow funds for the short-term due to the temporary shortfall in revenue generation. The government instead of cutting back on its spending may borrow funds from

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outside to tide over cash crunch in the revenue and the expenditure as predicted in the budget. These borrowings form parts of 'public debt' or 'government debt'. Each and every country adopts different debt management techniques depending upon its broader objectives like: a. Attracting adequate funds into government coffers b. Minimizing interest costs c. Achieve proper debt structure with regard to maturity and d. Maintain and achieve economic and social targets In the Indian context, Indian government uses different sources of finance to achieve its public debt target. The public debt can be categorized into a) internal debt and b) external debt. The internal debt obligations of the central government as on date are: ? Market loans: These loans have a maturity of 12 months or more at the time of issue. The government sells openly its securities through Reserve Bank of India. ? Bonds: This category consists of bonds such as gold bonds, rural development bonds or infrastructure bonds etc. ? Treasury Bills: These are short-term debt obligations created to bridge a gap between revenue and expenditure. ? Ways and Means Advances from RBI: These are advances taken from Reserve Bank of India to meet short-term obligations. This debt is purely temporary in nature and usually paid within three months. ? Securities against small savings: Under this mechanism, substantial part of small securities is converted into central government securities. ? Small savings from Public: Through innovative schemes such as National Saving Scheme etc., government mobilizes funds on a continuous basis through post offices. ? Provident funds: These funds are segregated into employee provident fund and public provident fund. ? Reserve Funds and deposit funds: These are funds deposited with the central pool of funds by Railways and other public sector undertakings. The external debt obligations of the central government as on date are: 1. Foreign currency loans from developed countries like USA, UK, France, Former USSR, Germany, Japan etc. 2. Foreign currency loans from international financial institutions like IMF and IBRD etc.

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At this juncture, one has to understand Reserve Bank of India plays a pivotal role in mobilizing debt and repayment of public debt on behalf of the government. Reserve bank indirectly uses the government debt instruments and T-Bills in its open market operations (OMOs) of buying and selling these securities to achieve price stability in the economy by controlling the money supply in the economy. These open market operations are also taken up to see that bond yields in the economy are normal or to see that a yield curve is normal. A yield curve is a line that plots the interest rates with different maturities having equal credit quality. The central banks usually want to see that longer maturity bonds have a higher yield compared to shorter bonds due to the risks connected with time. (In a normal yield curve, the slope will move upward to depict higher yields often associated with long-term bonds). With regard to financial institutions, and banks, they borrow long-term funds to increase their balance sheet size and borrow short-term funds to tide over liquidity mismatches between cash inflows and cash outflows. The liquidity is all about the ability of the institution to meet its liabilities exactly when they are due. Long-term funds are needed for growth and short-term funds are needed for liquidity and short-term solvency. The businesses on the other hand require long-term funds to build their productive capacities and short-term funds to fund working capital needs of the organization. Both these funds are required for profitability, growth, liquidity and solvency. Financial prudence is to use the concept of financial leverage by using the mix of debt and equity in decreasing the cost of funds.

13.8 Short-term Financial Instruments

The short-term financial instruments that are used to fund the short-term fund requirements of Corporates and Government can be classified as follows:

13.8.1 Treasury Bills

Treasury Bills are short-term, rupee denominated instruments

100%

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issued by the Reserve Bank of India (RBI) on behalf of the Government of India.

65%

MATCHING BLOCK 146/173

SA

Chapter 4 IFS MONEY MARKET final.docx (D156861167)

Reserve Bank of India (RBI) on behalf of the Government of India. T-bills are issued

in the form of promissory notes or finance bills.

Features These short-term instruments are highly liquid and virtually risk-free. These are the most liquid instruments after cash and call money.

71%

MATCHING BLOCK 147/173

SA

Major Project Report_07416688519.docx (D110634119)

The Reserve Bank of India acts as a banker to the Government of India.

RBI acts as issuing agent. Treasury bills are raised to meet the short-term requirements of Government of India.

T-bills are issued either in the form of promissory note (or scrip) or credited to investors'

Subsidiary General Ledger (SGL) account.

94%**MATCHING BLOCK 149/173****SA**

Shivani Sharma, final thesis.pdf (D30330450)

Bids for treasury bills are to be made for a minimum amount of ₹ 25,000 and in multiples thereof.

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Yield T-bills do not carry a coupon rate, but they are issued at a discount. Yields on T- bills are considered as benchmark yields. The yield on T-bill can be calculated as under $\text{Yield} = \frac{\text{Face Value} - \text{Price}}{\text{Price} \times \text{Days}} \times 365$

Types of Treasury Bills Treasury bills are issued at various maturities,

85%**MATCHING BLOCK 148/173****W**

generally up to one year. Thus, they are useful in managing short-term liquidity.

At present, the GOI (Government of India) issues 3 types of T-bills viz., 91-day, 182-day and 364- day. Ad hoc T-bills are issued in favor of the RBI when the Government needs cash. These bills are purchased by RBI at discount. Issuing Procedure or Auctioning of Treasury Bills Treasury Bills are issued by auctioning techniques. The issuing procedure of auctioned T-bills is discussed below: ? The bills are sold by the RBI, Public Accounts Department (PAD), Mumbai, on an auction basis. ? Eligible investors intending to procure the instruments need to submit their tender for the issue of bills in the form as prescribed for the purpose. ? Successful competitive bids will be accepted up to the minimum discounted price called 'cut-off' price determined at the auction. ? Result of the auction is displayed at RBI. Appraisal of Treasury Bills Commercial papers, certificates of deposits, short term debentures and inter- corporate deposits are alternatives to treasury bills. Though T-Bills have low return they constitute a viable investment opportunity because of its benefits which are as follows: ? No tax deducted at source ? Eligibility for reserve requirements ? Insignificant capital erosion ? Zero default risk being sovereign paper ? It's a highly liquid money market instrument ?

80%**MATCHING BLOCK 151/173****SA**

Shivani Sharma, final thesis.pdf (D30330450)

Transparency in operations as the transactions would be put through RBI's SGL

account ? Simplified settlement ? Market related yields

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Treasury Bills in International Markets A brief discussion on treasury bills in international markets is given below: T-bills are important money market instruments in the US. In US, the minimum denomination of T-bills is USD100, and thereafter in multiples of USD100. Formerly USD 1000, and is now USD 100 with effect from April 2008. In UK too, the treasury bills are issued in the market by the government through the debt management office. T-bills are issued with maturities of 1 month, 3 months, 6 months and 12 months.

13.8.2 Commercial Paper

Market

Commercial Paper (CP) is an unsecured usance money market instrument issued at a discount

in the form of a promissory note, and is transferable by endorsement and delivery and is of fixed maturity.

Companies, All-India Financial Institutions (FIs) and Primary Dealers (PDs) can raise funds through the Commercial Paper. The individuals, banking companies, other

corporate bodies registered or incorporated in India and unincorporated bodies, (

NRIs and Foreign Institutional Investors (FIIs)

can buy them. Commercial paper has a minimum maturity period of seven days and a maximum of one year. Unlike Commercial

Deposit (CD), the issuer can buy- back its CP. CPs are

issued at a discount to face value as may be determined by the issuer.

CPs are issued in denominations of ` 5 lakh or multiples thereof. Features of Commercial Paper Commercial paper favors both borrowers and investors. It is considered as an optimal combination of liquidity and returns in the short-term market. 1.

CPs are backed by the liquidity and earning power of the issuer, but are not backed by any

assets, and they are unsecured. 2. The CP market provides the borrower (i.e., highly rated corporates) a cheaper source of funds with

less paperwork. 3. Investors prefer to invest in CPs due to high liquidity 4. It is a short-term maturity with a minimum maturity of

seven days and maximum maturity of one year. Issuing Procedure of Commercial Paper 1. A corporate planning to issue CP requires

fulfilling the eligibility criteria prescribed by the RBI 2. Once it satisfies the eligibility criteria it needs to select a merchant banker and

an issuing and paying agent (IPA). Generally, banks act as Issuing and Paying Agents (IPAs) 3.

All eligible participants have to obtain the credit rating from

specified rating agency.

The minimum credit rating should be A2 as per rating symbol and definition prescribed by

SEBI.

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The merchant banker on behalf of the corporate client, will locate the clients and get their quotes for different maturity periods as discussed above. Then the company and merchant banker / IPA decide the maturity, discount rate and the quantum of the issue. 6.

On maturity, the holder of the CP presents the instrument to the paying agent. Pricing of Commercial Paper The CPs are issued to the investors at a discount to the face value. The discount actually is the effective interest rate. The Issue Price is determined by the corporate issuing it in the following manner: The issue price can be calculated as

under:
$$F P = I \times N \frac{1}{1 + 100 \times 365}$$
 Where, F = Face/Maturity Value P = Issue Price of CP I = Effective Interest p.a. N = Usance Period (No. of days).

Advantages of Commercial Paper The paper work involved in raising the funds through the Commercial Paper is very less because more funds can be procured without any underlying transaction. The flexibility provided by the instrument, enables the company to raise additional funds especially when the market is favorable. Evolution and Development of Commercial Paper The concept of raising funds through commercial paper was new to Indian corporates. The introduction of CPs is a result of the suggestions of the Working Group on Money Market in 1987. In 1989, the RBI announced its decision to introduce CPs. But, CP market has not developed as anticipated because of stringent conditions laid by the RBI to issue such instrument, cost of issuing CPs and minimum size of investment for an investor to buy the instrument. The commercial paper market in India started to grow from 1997 -98. However, the actual growth began after the financial crisis of 2008, with the number of issues increasing five-fold in five years. Post-financial crisis, the Reserve Bank of India, between 2008 to 2011, reduced the repo rate from 9% to 4%. The bank lending rate did not follow suit and thus hovered around 12%. But, the discount rate of Commercial Paper was around 6.5% to 10%, lower the bank lending rate. This prompted many corporates to embark on the CP route as this was a cheaper form of finance than the working capital finance from the banks.

Block IV: Financial Management 174 Table 13.1. Commercial Paper Market – July, 2020 to July, 2021 Date: Sep 16, 2021 Item 2020 2021 Jul. 31 Jun. 15 Jun. 30 Jul. 15 Jul. 31 1 2 3 4 5 1.

100%	MATCHING BLOCK 150/173	W
Amount Outstanding (₹ crore) 374817.20 404804.90 376117.85 471218.00 414981.65 1.1 Reported during the fortnight (₹ crore) 53608.10 73440.40 97928.00 117197.20 149052.15 2. Rate of interest (per cent) 3.18-12.33 3.36-11.32 3.43-13.03 3.32-12.80 3.38-12.94		

https://www.rbi.org.in/Scripts/BS_ViewBulletin.aspx?Id=20531

Commercial Papers in International Markets Commercial paper has been recognized as an important means of financing working capital by US companies since the 18th Century.

The use of commercial paper has been adopted by every state in the United States except Louisiana. Outside US, the international Euro – commercial paper market is the largest with over USD 500 billion. It is denominated by Euros, dollars and Sterling pounds. Today, CPs are the second largest money market instrument in the US after Repos. In UK, the Commercial Paper (CP) is regarded as a flexible short- term instrument through which a cost-effective funding of requirements can be done. 13.8.3 Certificate of Deposits The RBI introduced Certificates of Deposit (CDs), in 1989 based on the Vaghul Committee recommendations. Certificates of Deposit (CDs) are the instruments issued by banks in the form of usance promissory notes. These bank deposits are negotiable, and are in marketable form bearing specific face value and maturity.

Scheduled commercial banks, selected all India financial institutions are permitted by RBI to issue CDs for raising short-term resources.

CDs are available to individuals, corporations, companies, trusts, funds, associations, etc., for subscription. Non-resident Indians can also subscribe to these instruments.

The

weekly settlement data of certificate of deposits is shown in Table 13.2 below:

Unit 13: Sources of Long-term and Short-term Finance 175 Table 13.2: Weekly settlement data – July 30, 2021 to Aug 13, 2021 Date:

Sep 10, 2021 Certificate of Deposit Fortnight Amount Outstanding (₹ crore) During the Fortnight

Amount Issued Rate of Interest (Per cent) 1 2 3 Jul 30, 2021 64304 951 4.05-4.85 Aug 13, 2021 63489 73 4.31-4.31

https://www.rbi.org.in/Scripts/BS_ViewBulletin.aspx?Id=20531

Features of CDs The distinct features of CDs are: ? Minimum Size and Denomination: CDs are form of small investments. CD should be issued in denomination of ₹ 1 lakh (1 unit) of Maturity Value (MV) / Face Value (FV). CD is a document of title to a time deposit and is distinct from conventional time deposit with respect to negotiability and marketability. ? Term/Maturity: CDs are short term investments. Banks can issue CDs for a minimum period of seven days to a maximum of one year. The liquidity and marketability features are considered as the hallmarks of CDs. ?

CDs

are issued at a discount to face value. The discount rate

is

calculated as follows: ? ?

F DR

I

x N 1 100x365 ? ?

Where, DR = Discounted value N = Issuance period F = Face value I = Effective interest rate

per annum. ? CDs are freely transferable by endorsement and delivery.

Purpose of Issue CDs benefit both issuers and investors. From the issuers (banks) point of view, CDs are issued foreseeing the advantages over conventional deposits. The motives behind issuing CDs are control over cost of funds and assured availability of funds. Procedure of Issue of CDs The investor will make an application to the issuer for investing in the CD. CDs are issued in demat form only. CDs are issued in physical form, only on request of the investor.

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Maturity and Payment

Banks are not permitted to buy back their CDs prematurely, nor allowed to grant loans against CDs.

Negotiability of CDs Different kinds of CDs are issued by banks and other depository institutions. But, negotiable CDs are considered as true money market instruments. Negotiable CDs are issued in bearer form and are registered in the books of the issuing depository institution in the name of the investor. Since they are issued in bearer form, trading in the secondary market becomes more convenient for an investor. Negotiable Certificates of Deposit (NCDs) are tradable time deposits. Most NCDs carry a fixed rate of interest till maturity. However, a few NCDs are now being issued with variable interest rates, where the period of the instrument is divided into equal sub-periods and the rates are decided at the beginning of each sub-period

13.8.4 Bills of Exchange Commercial bill had its origin in Europe as an early medieval financial innovation evolved over centuries from a personal bond executed by debtor before a court or a public notary to its present form of a commercial financial instrument. In India too, indigenous bankers and other business houses have been historically using some kind of Bill-like instruments written in vernacular languages, known as 'Hundies' in their many variants to pay and receive the value of goods exchanged in the course of trade. However, with the development of organized financial markets over the years, and the spread of commercial banking, the role of indigenous bankers in the financial system diminished in importance and Hundies too gradually started losing their status as the principal instrument of credit and were replaced by bill of exchange in its present form.

96%

MATCHING BLOCK 152/173

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Section 5 of the Negotiable Instruments Act, 1881, defines Bills of Exchange as 'an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument.'

96%

MATCHING BLOCK 153/173

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Section 5 of the Negotiable Instruments Act, 1881, defines Bills of Exchange as 'an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument.'

Parties to a bill of exchange –

drawer, drawee and payee. The maker of the instrument who directs to pay is the drawer, the person to whom the direction is given is the drawee (when he accepts the bill, he becomes the acceptor) and the person to whom payment is to be made is the payee. In some cases, the drawer and the payee may be the same person.

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Classification of Bills of Exchange There are various types of bills of exchange in vogue today in the market: (a) They can be classified as 'demand' and 'usance' bills on the basis of when they are due for payment, i.e., immediately, 'at sight' or 'on presentation', as in case of demand bill or at a specified later date (usually three months) as in case of an usance bill. (b) Bills again are classified as 'documentary' when they are accompanied by documents of title to goods such as railway receipts / lorry receipts / bills of lading, etc., or "clean" when not accompanied by such documents. (c) Some bills are classified as 'D/A' and 'D/P' bills on the basis of whether the documents are Deliverable just against Acceptance (

D/A) or Deliverable only against Payment (D/P), usually through a bank. A D/A bill, however, becomes a clean bill immediately after the delivery of the documents. (d) Bills are classified as 'Inland' and 'Foreign.' Inland bills

must be drawn or made in India, and must be payable in India or drawn on any person resident in India.

On the other hand, foreign bills are drawn outside India and may be payable in and by a party outside India or are drawn in India and made payable outside India. A related classification of bills is export bills and import bills. While export bills are those drawn by exporters in India on any country outside India, import bills are those drawn on importers in India by exporters outside India. (e)

Besides, there are 'supply bills', 'government supply bills' and 'accommodation bills'. The supply bill arises out of supply of goods by manufacturing concerns and the government supply bills arise out of the supply of goods to the government or any of its departments. (f) With regard to international trade, bills are classified into four categories. They are Bill discounting backed with LC

(LCBD); Clean Bill Discounting (CBD); Invoice Bill Discounting (with recourse) and Invoice Bill Discounting (without recourse) The Letter of Credit bill discounting is a short term credit facility provided by the bank by purchasing the letters of credit and in return

make an advance payment to the seller/exporter. In case of clean bill discounting, the working capital finance is provided by discounting clean bills i.e., bills which are not accompanied by any documents such as railway receipt, lorry receipts etc. Invoice bill

discounting with recourse means the seller has to bear the debt in case the debtor does not pay the money; while such a facility doesn't exist for without recourse invoice discounting. An accommodation bill is the one accepted by the drawee to accommodate

the drawer without having received any consideration. Banks have to be cautious while extending credit against accommodation bills as they are prone to frauds, also known as kite flying.

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Steps in Bill Financing Bill financing involves discounting and purchasing of commercial bills arising out of sales. The characteristic of

easy transferability of the bill was the key feature of the instrument, it enabled the bill to be assigned to a bank for the drawer to obtain cash immediately and thus, evolved the practice of discounting of bills. A further landmark in the evolution of bill was its being

accorded the characteristic of negotiability. How does a bill of exchange come into existence? Suppose, seller A sells goods to buyer B on credit but wants to have money immediately, he draws a bill of a given maturity on B and sends

the bill to B. A is known as the drawer of the bill and B, the debtor, acknowledges his responsibility for the payment of the amount on terms mentioned on the bill, by writing on the bill his "acceptance". When B has "accepted" the bill, he

is known as the acceptor or drawee of the bill. A, in need of immediate money takes

the "accepted bill" to a bank which exchanges it for ready money. This act of handing over the endorsed bill in exchange for ready money is called "discounting the bill of exchange". The difference between the money paid to the seller or creditor or drawer of the bill and the amount of the bill is called the "discount" which is calculated at a rate per cent per annum on the maturity value.

Benefits and Costs of Bill Financing The bill financing has its own benefits and costs. Benefits of Bills Finance Following are some of the major benefits to the banks providing bills finance: ? Self-liquidating mode of financing ? Liquidity management of the banks becomes easier. ? Easy to monitor the genuineness of the transactions. ? Monitoring of borrowers' receivables becomes easy. ?

Quality of receivables can be ascertained. ? Bank has recourse, both to the drawer as well as the drawee. ? Sale transactions are

routed through the bank. ? Effective yield is higher since discount is deducted upfront. ? Facility of rediscounting ? Disciplined way of financing. Costs of Bills Finance The usage of Discounting of Bills is not free of costs. The following are some of the costs associated

with the discounting of bills. i. Operational and Procedural Constraints – These include wide geographical spread of the buyers, procedural delays on the part of both the

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drawer's and the drawee's banks, cumbersome documentation formalities, difficulties in submitting supporting documents, banks are hesitant to discount bills on new buyers etc. ii. Difficulties Experienced in Getting Bills Accepted – There are cost related difficulties in getting usance bills accepted by the customers. Also the reluctance on the part of the buyers and the formalities involved act as a hindrance. iii. Discounting of Bills with Banks Cumbersome - The procedure for discounting of bills with banks was cumbersome. This apart the banks may not accept every bill because of credential of the drawer of the bill. iv. Dishonor of Bills - The major reasons for dishonor of bills are: Buyers do not have funds; Return of the materials; deliberate dishonor; adverse business conditions. A majority of the respondents (56%) felt that the existing laws were not sufficient to deal with the defaulters. v. Payment of Bills –The existing bank mechanism for payment of bills is considered inadequate by most of the bankers. Rediscounting of Bills of Exchange Banks can rediscount the bills, which were originally discounted with them by their corporate clients, with eligible financial institutions. The only prerequisite is that the originally discounted bills should have arisen out of genuine trade transactions. Banks compute the total amount of eligible bills discounted by them after deducting the rediscounts already booked on the bills and approach the approved rediscounting institutions to verify the availability of funds and the prevailing rate. Bill Market in India With the dominance of cash credit system in financing domestic trade and industry, bill finance, despite its inherent advantages from the point of view of the lending banker, has been relegated to play only a marginal role in the credit delivery system of the country. The need for the development of bill culture among borrowers was stressed by the various committees, appointed by the Government of India and the Reserve Bank of India, while examining certain aspects pertaining to bank lending / money market / banking sector reforms. The committees, which had gone into the different aspects of working capital financing, stressed the need to promote the Bill culture, so as to inculcate some measure of financial discipline among borrowers. Even though the role of commercial bill market as an important component of the money market was recognized as early as in the 1930s, concerted efforts were not made in this direction till 1952. In fact, the bill market scheme of 1952 was floated in an altogether different context. The RBI's decision in November 1951 to hike the bank rate from 3% to 3.5% and to refrain from making open market purchases of government securities, save in special circumstances and at

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its discretion, closed the liquidity window that was available to commercial banks, under Section 17(4) (a) of the RBI Act, 1934, enabling them to tide over their seasonal liquidity pressures. The next significant measure taken by the RBI for promotion of a bill market was in November 1970 by the introduction of the New Bill Market Scheme (NBMS). The scheme was restricted to genuine trade bills only and provided for rediscounting of four types of bills having at least two good signatures, one of which had to be that of a licensed scheduled bank or a State Co-operative Bank. Factors behind Underdevelopment In spite of the encouraging official policy, the bill market has not developed in India. The factors responsible for its underdevelopment are: i. Borrowers have found other forms of financing such as cash credits, overdrafts, etc., cheaper to bill financing. ii. Bill markets were mostly established for the purpose of financing foreign trade. The share of foreign trade in the national income has remained quite small. iii. Participation of government in the economic activity has led to an increase in 'supply bills' but not that of genuine bills of exchange. iv. Bill market in India has been dominated by indigenous bankers whose funds were limited. v. Borrowings against bills are not wide spread. vi. There is no secondary market for already bills discounted by the banks. vii. The rediscounting of bills by RBI throughout the year is low ix. There is hardly any broker or dealer to support in Bills market 13.9 Working Capital Management

Working capital management is concerned with the problems that arise in attempting to manage the current assets, the current liabilities, and the interrelationship that exists between them. Assets and liabilities of a company can be classified on the basis of duration. Assets can be classified into fixed assets and current assets, while liabilities are classified as long-term liabilities and current liabilities on that basis. As a finance manager, you must be able to manage different components of both current assets and current liabilities. 13.9.1

Meaning and Need for Working Capital Working Capital represents the capital required by a business for operating its day-to-day trading activities. It is a financial barometer of the operating liquidity of a business. There are two concepts of working capital:

Working Capital Concepts **Gross Working Capital:** It represents the sum total of all current assets of a business. The current assets comprise inventories (including raw material and

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components, work-in-process and finished goods), receivables, loans and advances and cash and bank balances. These are short-term assets having a life span of less than one year. **Net Working Capital (NWC):** This concept of working capital is more popularly used as it represents the excess of current assets over current liabilities. It can be shown as: $NWC = \text{Current Assets (CA)} - \text{Current liabilities (CL)}$ The net working capital for a firm can be positive or negative. A positive NWC denotes that the firm can generate adequate funds from the current assets to repay its current liabilities. On the other hand, if the networking capital is negative, it shows that the business does not have sufficient funds to repay its liabilities. This might result in liquidity crisis for a business. Such a negative figure of working capital is also referred to as working capital deficit. The working capital deficit can be met with working capital finance from banks or financial institutions. **Working Capital Assessment Methods** To disburse working capital finance to businesses, banks adopt several methods for assessing the working capital requirements of a business. These methods are: 1. **Operating Cycle Method** – The operating cycle method is based on the length of time required to convert current assets into cash. This method is dealt with in greater detail in subsequent sections in the unit. 2. **Drawing Power Method** – Used for businesses that enjoy limited drawing powers.. Under this method, the finance requirement is assessed on the basis of valuation of current assets charged to the bank in the shape of hypothecation and assignment, after deducting the stipulated margin. 3. **Turnover Method** – This method was originally suggested by the Nayak committee to assess the working capital requirements for small-scale units. Based on the recommendations of this committee, the minimum working capital required is computed as 20% of the projected annual turnover for new as well as existing units. The borrower has to bring in 5% of the annual turnover as margin money. 4. **MPBF Methods** – In accordance with the recommendations of the Tandon Committee in 1974, RBI has framed two methods for assessing working capital. They are known as Method I and Method II. Under the first method, the MPBF (Maximum Permissible Bank Finance) should be 25% of working capital gap. The working capital gap is the excess of current assets over other current liabilities (excluding bank borrowings). Under method II, The MPBF should be 25% of total current assets (excluding exports receivables).

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Need for Working Capital Management There are three points of distinction between current assets and fixed assets – Time is a crucial factor for considering a fixed or long-term asset. It is due to this reason that the concepts of discounting and compounding assume important role in any capital expenditure decision. But because, the time-frame of current assets is only one accounting period, the time value of money

may be of less relevance in case of current assets. The liquidity position of a business is greatly influenced by the amount of money invested in current assets. Higher investment in current assets signifies higher liquidity. On the other hand, fixed assets do not affect the liquidity position of a business. Current assets management is vital as any short run, urgent need of cash for the company is satisfied only by varying the level and composition of current assets. Hence, efficient management of current assets becomes a part of management of working capital. 13.9.2

Objectives of Working Capital Management The basic objective of working capital is to provide adequate support for the smooth functioning of the normal business operations of a company. The question then arises as to the determination of the quantum of investment in working capital that can be regarded as 'adequate'. Once we recognize the fact that a company has to operate in an environment permeated with uncertainty/risk, the term 'adequate working capital' becomes somewhat subjective depending upon the attitude of the management towards uncertainty/risk.

This requires prudent working capital management practices. **Liquidity Vs. Profitability**

The quantum of investment in current assets has to be made in a manner that it not only meets the needs of the forecasted sales but also provides a built-in cushion in the form of safety stocks.

Such a safety stock net helps

to meet unforeseen contingencies arising out of factors such as delays in arrival of raw materials, sudden spurts in sales, demand etc. Consequently, the investment in current assets for a given level of forecasted sales will be higher if the management follows a conservative attitude than when it follows an aggressive attitude. Thus a company following a conservative approach is subjected to a lower degree of risk than the one following an aggressive approach. Further, in the former situation the high amount of investment in current assets imparts greater liquidity to the company than under the latter situation wherein the quantum of investment in current assets is less. This aspect considers exclusively the liquidity dimension of working capital. There is another dimension to the issue, viz., the 'profitability' and it is discussed below.

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Once we recognize the fact that the total amount of financial resources at the disposal of a company is limited and these resources can be put to alternative uses, the larger the amount of investment in current assets, the smaller will be the amount available for investment in other profitable avenues at hand with the company. A conservative attitude in respect of investment in current assets leaves less amount for other investments than an aggressive approach does. Further, since current assets will be more for a given level of sales forecast under the conservative approach, the turnover of current assets (calculated as the ratio of net sales to current assets) will be less than what they would be under the aggressive approach. This being so, even if we assume the same level of sales revenue, operating profit before interest and tax and net (operating) fixed assets, the company following a conservative policy will have a low percentage of operating profitability compared to its counterpart following an aggressive approach as can be seen from the numerical illustration 13.1.

Illustration 13.1

S.No.	Particulars	Conservative Policy	Aggressive Policy
1.	Net Sales	50 lakh	50 lakh
2.	Operating Profit Before Interest and Tax	5 lakh	5 lakh
3.	Net (Operating) Fixed Assets	10 lakh	10 lakh
4.	Current Assets	8 lakh	5 lakh
5.	Total Operating Assets [= (3) + (4)]	18 lakh	15 lakh
6.	Net Operating Profit Margin (2) = (1) ? ? ? ? ? 5	=10%	50 5 =10%
7.	Turnover of Net Operating Fixed Assets (1) = (3) ? ? ? ? ? 50	=5 times	10 50 =5 times
8.	Turnover of Current Assets (1) = (4) ? ? ? ? ? 50	=6.25 times	8 50 =10 times
9.	Turnover of Total Operating Assets (1) = (5) ? ? ? ? ? 50	=2.78 times	18 50 =3.33 times
10.	Rate of Return on Total Operating Assets [= (6) x (9), (2) x 100 (5)]	27.8%	33.3%

Contd....

Block IV: Financial Management 184 11.

Ratio of Current Assets to Net Operating Fixed Assets (4) = (3) ? ? ? ? ? 8 = 0.8 10 5 = 0.5 10 = 80% = 50%

From the illustration, it can be easily seen from item (10), that the alternative of following a conservative approach to investment in current assets results in a low profitability of 27.8

per cent compared to the profitability of 33.3 per cent

obtained under the alternative – an aggressive approach. The reason for this can be directly traced to the low turnover of current assets leading to a lower turnover of total operating assets under the conservative approach compared to that under the aggressive approach. From item (11), it can be seen that current assets comprise 80 per cent of net operating fixed assets resulting in higher proportion of current assets and hence greater liquidity compared to the corresponding figure of 50 per cent indicating low liquidity under the aggressive approach. From the above discussion it is apparent that management of current assets inevitably leads to a trade-off between 'profitability' and 'liquidity'. An aggressive approach results in greater profitability but lower liquidity while a conservative approach results in lower profitability but higher liquidity. This can be resolved to a certain extent by the management by following a moderate policy which is neither highly aggressive nor highly conservative. Under this approach, some liquidity and some profitability have to be sacrificed so that the resultant figures of liquidity and profitability are reasonably satisfactory to the company. For example, in the numerical illustration given earlier, if the management decides to follow a moderate approach which leads to an investment of ` 6.5 lakh in current assets, then the rate of return of total operating assets will become 30.30

per cent 5 16.5 ? ? ? ? ? which is higher than

the rate of return of 27.8 per cent under the conservative approach but lower than the figure of 33.3 per cent under the aggressive approach. Further, the degree of liquidity as indicated by the ratio of current assets to net operating fixed assets will now be 65 per cent

which is lower than the figure of 80 per cent under the conservative approach but higher than the figure of 50 per cent under

the aggressive approach. Thus, a proper balancing between liquidity and profitability can be reached by considering alternatives along with their consequences on liquidity and profitability. Among the alternatives the one which matches the attitude of the management towards risk can be selected. Choosing the Pattern of Financing In the

normal course of business, a company will usually have access to non- interest bearing short-term liabilities such as sundry creditors, accrued expenses

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and other current liabilities as also provisions towards financing current assets. These are called spontaneous liabilities as they arise more or less automatically in the context of current assets. The difference between the amounts of current assets and spontaneous liabilities needs to be financed by a combination of bank borrowings in the form of cash credit/overdraft arrangement and long-term sources of finance such as debentures and equity capital. Fixed deposits obtained from the public for periods ranging from one to three years can also be used for the same purpose. Here also an aggressive financing policy will tend to have a financing mix tilted in favor of bank borrowings and public deposits compared to a conservative policy tilted more towards long-term sources like equity, and to some extent debentures. Except in rare instances, the general tendency in the case of manufacturing and trading companies is that during certain periods in a year, the need for current assets will be much higher than in other periods in the year. As the financing charges in the case of bank borrowings are geared to and move in tandem with the credit needs occasioned by the higher investment in current assets, the total interest charge is likely to be low. However, debt-servicing cost will be high as bank borrowings have to be repaid (rather re-negotiated for the coming year). Consequently, the risk of 'technical insolvency' (a situation where a company is not in a position to honor its current liabilities including short-term bank borrowings which can arise even in the case of profitable companies) is likely to be high. On the other hand, a conservative policy having a high proportion of equity capital and to some extent debentures will have comparatively low debt-servicing resulting in a lower degree of the risk of technical insolvency. However, the cost of financing will be high as the cost of equity capital is the highest and it does not provide tax benefit which the interest on borrowed capital provides to the company and debenture interest (even after reckoning with tax benefit) has to be paid throughout the year irrespective of the fluctuating credit needs of a company towards financing its current assets. Even in the case of choosing the mix of instruments for financing current assets, the risk of technical insolvency tends to be high while the cost of financing tends to be low under an aggressive policy compared to a conservative policy under which the risk of technical insolvency will be low while the cost of financing tends to be high. Once again, the management's attitude towards risk will go a long way in determining the financing-mix considered appropriate to the company.

From the above discussion it emerges that working capital management encompasses the management of current assets and the means of financing them. The objective of working capital management is to balance the 'liquidity' and 'profitability' criteria while taking into consideration the attitude of management towards risk and the constraints imposed by the banking sector while providing short-term credit in the form of cash credit/bank overdraft.

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Factors affecting Composition of Working Capital

Some of the significant factors affecting the composition of working capital or current assets are: Nature of Business Purely trading organizations will have basically finished goods inventory, accounts receivable (in some cases) and cash as current assets and accounts payable as current liabilities. Similarly, travel agency firms will have predominantly accounts receivable and some amount of cash as current assets unlike manufacturing and trading companies. The investment in net (operating) fixed assets²¹ will at most be around 5

per cent

of investment in current assets. On the other hand, capital goods manufacturing and trading companies will have a high proportion of current assets in the form of inventory of raw materials components and work-in-process. The ratio of net (operating) fixed assets to current assets will be around 100 per cent or more.

Nature of Raw Material Used The nature of major raw material used in the manufacture of finished goods will greatly influence the quantum of raw material inventory. For example, if the raw material is an agricultural product whose availability is pronouncedly seasonal in character the proportion of raw material inventory to total current assets will be quite high. For example, tobacco is the major raw material for cigarette industry whose availability is seasonal in nature and also the tobacco procured requires a reasonably long 'curing' period. Consequently, the percentage of raw material inventory to total current assets will be quite high compared to other items. Similarly, companies using imported raw materials with long lead time tend to have a high proportion of raw material inventory. In the case of capital goods manufacturing company, the demand for whose product is growing over time, the tendency will be to have high inventory of raw materials and components.

Process Technology Used In case the raw material has to go through several stages during the process of production, the work-in-process inventory is likely to be much higher than any other item of current assets.

Nature of Finished Goods The nature of finished goods greatly influences the amount of finished goods inventory. For example, if the finished goods have what is called a short span of 'shelf-life', as in the case of cigarettes, the finished goods inventory will constitute a very low percentage of total current assets. 21

The

term net (operating) fixed assets consists only of net fixed assets that are being used for the normal business operations of a company and will not include capital work-in-progress as the latter cannot be used for the present operations of the company.

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In the case of construction companies, which undertake work on a turnkey basis, as soon as the construction is completed, the customer will take possession of it. Consequently the finished goods inventory will be virtually insignificant and the work-in-process inventory (rather work-in-process) will be considerably high. In the case of companies the demand for whose finished goods is seasonal in character, as in the case of fans, the inventory of finished goods will constitute a high percentage of total current assets. This is mainly because from the point of view of fixed costs to be incurred by the company, it would be more economical to maintain optimum level production throughout the year than stepping up production operations during busy season. In the case of reputed companies, manufacturing consumer goods that enjoy growing demand over the years, the finished goods inventory need not be high as sales demand can be forecast with a reasonable degree of accuracy. However, in such companies the raw material inventory tends to be high in view of the large variety of products to be manufactured.

Degree of Competition in the Market The composition of

working may undergo a change due to increased competition. To face the competition, companies may offer extended credit period to the customers and may also lower their credit standards. An increase in credit period will directly influence the current assets by increasing the accounts receivable balance.

13.9.4 Operating Cycle Approach to

Working Capital Inter-dependence among the various components of working capital can be easily understood from Figure 13.1 given below: Figure 13.1:

Working Capital Cycle (Operating)

Source: ICFAI Research Center

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Figure 13.1 depicts the inter-dependence among the components of working capital. A company starting with cash purchases raw materials, components etc., on a cash or credit basis. These materials will be converted into finished goods after undergoing the stage of work-in-process. For this purpose, the company has to make payments towards wages, salaries and other manufacturing costs. Payments to suppliers have to be made on purchase in the case of cash purchases and on the expiry of credit period in the case of credit purchases. Further, the company has to meet other operating costs such as selling and distribution costs, general, administrative costs and non-operating costs described as financial costs (interest on borrowed capital). In case the company sells its finished goods on a cash basis, it will receive cash along with profit with least delay. When it sells goods on a credit basis, it will pass through one more stage, viz, accounts receivable and gets back cash along with profit on the expiry of credit period. Once again the cash will be used for the purchase of materials and/or payment to suppliers and the whole cycle termed as working capital or operating cycle repeats itself. This process indicates the dependence of each stage or component of working capital on its previous stage or component. The dependency of one component of working capital on its previous stage/component is described above in Figure 13.1.

However, there can be other kinds of inter-dependence which are not dictated by the usual sequence of manufacturing and selling operations. For example, in case the manufacturing process may require a raw material which is in short supply, the company may have to make advance payment in anticipation of the receipt of that raw material. This will cause immediate drain on cash resources unlike a situation where credit purchase of raw materials can be made. Similarly, if there is an excessive accumulation of finished goods inventory, the company may have to provide more liberal credit period and/or relax its existing credit standards which will increase sundry debtors. In situations of greater need for cash,

to boost

cash resources, providing cash discount as part of credit-terms for sale may have to be resorted to. In such cases, the relative benefits and costs may have to be taken into consideration before taking decisions.

Check Your Progress – 2 6.

Which of the following is not a

current liability? a. Creditor b. Bank overdraft c. Outstanding expenses d. Hire purchase dues e. Debentures 7. Net working capital is the difference between a. Current Assets and Fixed Assets b. Current Assets and Current Liabilities

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c. Fixed Assets and Current Liabilities d. Long-term Liabilities and Current Liabilities e.

Current Assets and Long term liabilities 8. Which of the following is not a factor affecting the working capital requirement of an organization? a. Degree of competition in the market b. Nature of finished goods c. Process technology used d. Nature of raw

material e. Long-term sources of finance available 9. This

90%

MATCHING BLOCK 155/173

SA

003_Banking and Indian financial _16-7-13.pdf (D142522847)

is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument. Identify the instrument. a. Bill of Exchange

an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument.

b. Certificate of Deposit c. Commercial Paper d. Treasury Bill e. Bank Overdraft 10. Which of the following is not an internal debt obligation of the Government? a. Treasury Bills b. Ways and Means advances c. Foreign currency loans d. Securities against small savings e. Provident funds Activity 13.2 1. Discuss the various instruments that Government can use for funding its short-term debt. 2. Goldman Sachs launched an online bank aimed at households and small businesses. As part of this new venture, Goldman is also offering a five-year certificate of deposit at 2.0%, also much higher than the going rates at other large banks. What is a Certificate of Deposit? How is it useful as a short-term finance instrument?

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Summary ?

The financial needs of an organization can be broadly classified into two heads. Short-term financial needs, and long-term financial needs. Both these needs are financed either by short-term funds or long-term funds.

It is prudent for an organization to meet its long-term fund requirement from long-term sources of finance rather than short-term sources. ?

Long-term finance is absolutely essential for any operating concerns. ? Any company needs to have a lot of money for investing in long-term assets such as land and buildings, plant and machinery, technical know-how and working capital margin, and hence it needs long-term sources of funds to finance these investments as usage of short-term funds will only result in asset-liability mismatch and make the firm illiquid. ? There are three main sources of long-term funds – equity shares, preference shares, and debentures. ? Equity shareholders are the owners of the company and enjoy residual profits after having paid all the commitments including preference share dividend. Companies have no fixed obligation to pay dividends and hence equity offers perpetual capital with limited liability for repayment. ?

Preference shares are similar to equity, in that there is no obligatory payment and the dividends are not tax deductible. However, preference

share-holders

earn a fixed rate of return for their investments. They have a preference over equity

share-holders

to post-tax earnings in the form of dividends and assets in case of liquidation. ?

Debentures are marketable claims wherein the company promises to pay the holder a specified rate of interest for a certain period and repay the principal on maturity. These instruments are generally secured by a charge on immovable properties of the companies.

Interest paid on debentures is tax deductible and debenture holders have the first right to assets in case of liquidation. Debentures can be classified into non-convertible, partly- convertible, and fully-convertible debentures. ? A company can raise money using any of these instruments by going to the capital market. There are many ways of doing it. A company can go for a public issue, a rights issue, private placement, buyout deals or euro-issues for raising finances. ?

Governments borrow long-term funds to invest in public sector institutions of production or to build social infrastructure like schools, hospitals, roads etc. The government on the other hand may borrow funds for the short-term due to the temporary shortfall in revenue generation. ? The short-term financial instruments that are used to fund the short-term fund requirements of Corporates and Government, can be classified as follows – Treasury bill market, commercial paper market, certificate of deposits and bills of exchange.

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Working capital management is concerned with the problems that arise in attempting to manage the current assets, the current liabilities, and the inter- relationship that exists between them. 13.11

Glossary Bought-out-Deal is a deal in which

a group of investors buys out a significant proportion of the equity of an unlisted company, with an intention to divest by taking it public, within an agreed time-frame.

Cost of Preferred Stock is the rate of return that must be earned on the preferred stock-holders' investment to satisfy their required rate of return.

A debenture is a marketable legal claim whereby the company promises to pay its owner, a specified rate of interest for a defined period of time and to repay the principal at the specific date of maturity.

Ex-rights is the period when a new investor in the stock is not allowed to benefit from the rights offering.

Equity shares are instruments the holders of which are considered as the real

owners of the business. They enjoy the residual profits of the company after having paid the preference share-holders and other creditors of the company.

They are also known as ordinary shares. Internal Accruals refers to financing through internally which can be done through the depreciation charges and the retained earnings.

Preference shares are those shares the holders of which

have preference over equity share-holders to the post-tax earnings in the form of dividends; and assets in the event of liquidation.

Record Date is the date specified by an issuer of a security for the purpose of determining the holders who are entitled to receive the rights shares or other distributions. Red Herring Prospectus The prospectus filed to the SEBI is referred to as Red Herring Prospectus because it contains a clause in red stating that the company should not attempt to raise funds from the public without the prior approval of the authority.

Spontaneous Financing refers to the trade credit and other accounts payable that arise spontaneously in the firm's day-to-day operations.

Stock Exchanges are the

formal organizations involved in the trading of securities. Such exchanges are tangible entities that conduct auctions in listed securities.

Secured Premium Notes (SPNs) is a kind of NCD with an attached warrant.

The warrant attached to the SPN gives

the holder the right to apply for and get allotment of one equity share for ` 100 per share through cash payment.

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Term Loan is a loan which is generally repayable in more than one year and less than 10 years.

Technical Insolvency is the situation in which the firm can no longer honor its financial obligations. Although its assets may exceed its total liabilities, thereby indicating a positive net worth, the company simply does not have sufficient liquidity to pay its debts. Trade Credit refers to the inter-firm credit arising from credit sales. It is recorded as an account receivable by the seller and an account payable by the buyer.

Gross working capital is the total of current assets. Net working capital is the difference between the total of current assets and the total of current liabilities. 13.12

Self-Assessment Test 1.

Differentiate between a rights issue and a public issue. 2. List the expenses related with a public issue. 3. What is the effect of rights issue on the wealth of the share-holders of the company? 4. Rights issue and bonus issue are two different issues, though they increase the paid-up capital of the company. Justify. 5. Differentiate between cumulative and non-cumulative preference capital. 6. Explain the differences between non-convertible debentures and partly convertible debentures. 7.

Discuss conservative working capital policy vs. aggressive working capital policy. 8. What are the spontaneous sources of financing current assets? Describe them. 9. Cash is an idle asset, which earns no return. In spite of this fact, companies hold cash. Briefly explain the motives of holding cash by the companies. 10. What are the two important characteristics of current assets? What are their implications for working capital management? 13.13

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Answers to Check Your Progress Questions 1. (e) Issue of Treasury bills Issue of treasury bills a short-term financial instrument, and hence is not a type of issue of securities. 2. (a) Venture Capital The European Venture Capital Association describes it as risk finance for entrepreneurial growth oriented companies. It is investment for the medium- or long-term seeking to maximize medium-or long-term return for both parties. 3. (d) Access to funds is limited The advantages of private placement are easy access to any company, fewer procedural formalities, lower issue cost and access to funds is faster. Access to funds is limited is a disadvantage. 4. (c) It will increase if he exercises the right The wealth of share-holder will increase if he/she exercises the right. 5. (d) Commercial Paper Commercial Paper is a form of short-term finance 6. (e) Debentures Debentures are a long-term liability

Unit 13: Sources of Long-term and Short-term Finance 195 7. (b) Current Assets and Current Liabilities Gross working capital refers to current assets while net working capital refers to the difference between current assets and current liabilities. 8. (e) Long-term sources of finance available The factors affecting the working capital requirement are: nature of business, nature of raw material used, process technology used, nature of finished goods and degree of competition in the market. 9. (a) Bill of Exchange

93%

MATCHING BLOCK 156/173

SA

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Bill of exchange is defined as an instrument in writing, containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument. 10. (

100%

MATCHING BLOCK 159/173

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as an instrument in writing, containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument. 10. (

c) Foreign currency loans Foreign currency loans represent an external debt obligation of the government. All the others are internal debt obligations.

Unit 14 Basics of International Trade and Finance Structure 14.1 Introduction 14.2 Objectives 14.3 Need for International Finance 14.4 Meaning and Implications of Globalization 14.5 Integration of Financial Markets 14.6 International Trade 14.7 Role of EXIM Bank 14.8 Exchange Control Regulations- FEMA 14.9

Highlights of Foreign Trade Policy 14.10

Summary 14.11 Glossary 14.12 Self-Assessment Test 14.13 Suggested Readings/Reference Material 14.14 Answers to Check Your Progress

Questions 14.1

Introduction

Previous unit
discussed

on short-term financial needs, and long-term financial needs of the business entities. The need to avoid asset-liability mismatch was also discussed in the previous unit. We briefly discussed on features of some of the equity and debt instruments. Some details on government borrowing – short- term and long-term – were discussed in the previous unit.

International finance or international macro-economics is a wide subject that covers contemporary issues such as: Why was the INR (Indian Rupee) so volatile against the USD (US Dollar)? Should we liberalize our domestic capital markets to accept FDI (Foreign Direct Investment) and FPI (Foreign Portfolio Investment)? What is the impact of higher FDI and FPI on domestic inflation? Similarly, at a corporate level, finance managers of MNCs who try to maximize shareholder wealth by playing across geographical markets have to live with the harsh reality of varying tax rates, interest rates, inflation rates, and exchange rates of the host countries. The competitiveness of an MNC depends on how they manage their international finance function effectively. Hence, MNCs want
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to know answers to questions like: Should we invest in China? Should we serve US/European markets? In today's globalized world, international trade, investments and aid will influence the movement of exchange rates. Volatile exchange rates influence revenues, costs, cash flows, profits, and thereby the market capitalization (measure of shareholder wealth). Every student of finance should gain mastery over this subject of international finance as it deals with causal factors of changing exchange rates and its impact on global trade and investments. 14.2

Objectives After reading through the unit, the student should be able to: ? Outline the importance of

International Finance ? Define the meaning and implications of globalization ? Identify the need for integration of financial markets and recognize the benefits, costs and effects of integration of financial markets ? Define the objectives and main features of the Foreign Trade Policy (2015-20)

14.3 Need for International Finance

Financial management of a company is a complex process, involving its own methods and procedures. It is made even more complex because of globalization, which makes the global financial and commodity markets more and more integrated. The integration is both across countries as well as markets. Not only the markets, but even the companies are becoming international in their operations and approach. When a firm is a pure domestic play, it operates only in the home country, both for procuring inputs as well as selling its output; it needs to deal only in the domestic currency. As companies try to increase their international presence, either by undertaking international trade or by establishing operations in foreign countries, they start dealing with people and firms in various nations. Since different countries have different domestic currencies, the question arises as to which currency should be used to settle the trade. The settlement currency may either be the domestic currency of one of the parties to the trade, or may be an internationally accepted currency. This gives rise to the problem of dealing with a number of currencies. The mechanism by which the exchange rate between these currencies (i.e. the value of one currency in terms of another) is determined, along with the level and the variability of the exchange rates, can have a profound effect on the sales, costs and profits of a firm. Globalization of the financial markets also results in increased opportunities and risks on account of the possibility of overseas borrowing and investments by the firm. Again, the exchange rates have a great impact on the various financial decisions and their movements can alter the profitability of these decisions.

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Meaning and Implications of Globalization In this increasingly globalized scenario, companies need to be globally competitive in order to survive. Knowledge and understanding of different countries' economies and their markets is a must for establishing a company as a global player. This knowledge will help the company to cater to the different needs and demands of customers in the domestic and international markets. For instance, the New York Times commented that the General Electric is doing well in developing countries by selling air fleet and aiding their infrastructure development. By the time the market cools overseas, i.e. in developing countries, GE predicts that the domestic market, i.e. the United States, will be ready to buy again. Studying international finance helps finance managers to understand the complexities of the various economies. It can help them understand how the various events taking place the world over are going to affect the operations of their firms. It also helps them to identify and exploit opportunities, while preventing the harmful effects of international events. A thorough understanding of international finance will also assist the finance manager in anticipating international events and analyzing their possible effects on the firm. The finance manager would thus get a chance to maximize profits from opportunities and minimize losses from events which are likely to affect the firm's operations adversely. Companies having international operations are not the only ones which need to be aware of the complexities of international finance. Even companies operating domestically need to understand the issues involved. Though they may be operating domestically, some of their inputs (raw materials, machinery, technological know-how, capital, etc.), may be imported from other countries, thus exposing them to the risks involved in dealing with foreign currencies. Even if they do not source anything from outside their own country, they may have foreign companies competing with them in the domestic market. In order to understand their competitors' strengths and constraints, awareness and understanding of international events again gains importance. What about the companies operating only in the domestic markets, using only domestically available inputs and neither having nor expecting to have any foreign competitors in the foreseeable future? Do they need to understand international finance? The answer is in the affirmative. Globalization and deregulation have resulted in the various markets becoming interlinked. Any event occurring in, say Japan, is likely to affect not only the Japanese stock markets, but also the stock markets and money markets the world over. For example, the forex and money markets in India have become totally interlinked now. As market players try to profit from the arbitrage opportunities arising in these markets, the events affecting one market also end up affecting the other

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market indirectly. Thus, in case of occurrence of an event which has a direct effect on the forex markets only, the above mentioned domestic firm would also feel its indirect effects through the money markets. The same holds good for international events, thus, the need for studying international finance.

14.5 Integration of Financial Markets To an investor, integration of financial markets means the freedom to invest or raise funds across different markets through various financial instruments. The advent of globalization has resulted in quick dissemination, money transfers and reduced transaction costs. Technology has played a key role in this process. As a result of financial integration, any factor affecting one market automatically affects the rest of the globe in no time. This effect is referred to as the transmission effect. Due to increase in inflation levels of different countries, the price of various financial assets varied with regard to change in domestic inflation rates as well as interest rates of various countries. These developments resulted in the development of new financial instruments, namely, interest rate swap, currency swap, futures, options, etc. It also led to liberalization of various regulations governing the financial markets and helped the countries in increasing international perspective with regard to different factors which create an impact on globalization. Benefits and Costs Effective integration of financial markets demonstrates better transfer of resources between surplus units and deficit units. Capital-rich countries experience lower return on capital compared to capital-poor countries. On the other hand, integration also involves risks such as currency risk, country risk, market risk and other kinds of risks. Variation in the value of investment in terms of domestic currency, denoted in other countries' currency is known as currency risk. It arises when the investor is unable to disinvest at will because of a country's sudden change in attitude towards foreign investment or any other factor such as war. Increase in volatility is the effect of globalization and integration of financial markets. Interest rates, exchange rates, etc., keep changing regularly because of the changes occurring in different segments of various financial markets in the world.

Check Your Progress – 1

1. Which of the following statements is true regarding international finance?
 - a. Companies having international operation only need to understand international finance.
 - b. Foreign companies situated in domestic markets only need to understand international finance.
 - c. Domestic companies having stake in foreign companies need to understand international finance.
 - d. Foreign companies having stake in domestic companies need to understand international finance.
 - e. All companies need to understand international finance.
2. Which of the following is/are settlement currency between international parties to trade?
 - a. Domestic currency of any one of the parties only
 - b. US Dollars only
 - c. Euro only
 - d. Internationally accepted currency only
 - e. Both domestic currency and internationally accepted currency
3. Which of the following statements is true with regard to diversification of securities?
 - a. Securities are negatively correlated.
 - b. Securities are not correlated.
 - c. Securities are perfectly correlated.
 - d. Securities are disproportionately correlated.
 - e. Securities are proportionately correlated.
4. Which of the following implies, 'integration of financial markets across geographical boundaries'?
 - a. Liberalization
 - b. Market integration
 - c. Globalization
 - d. Privatization
 - e. Nationalization
5. Which of the following is not a financial instrument that has evolved out of Globalization?
 - a. Currency swap
 - b. Interest rate swap
 - c. Futures
 - d. Options
 - e. Debentures

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14.6 International Trade A well-developed global financial system is essential for supporting increased international trade. The international payment system, the availability of international credit and credit guarantees (all forming a part of the international financial system), form the backbone of international trade. International trade

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of International Trade and Finance 201 theories can be seen as a measure to solve a nation's economic problems. Adam Smith advocated free trade as it leads to economic welfare of the society. Trade theories explain the characteristics of trading countries and from that they deduce: Why does a country engage in an international trade? Why does a country specialize in a certain kind of commodity exports or imports? What are the effects of trade on the domestic economy? Why is the intensity of trade more between any pair of countries? Should a country promote exports and avoid imports? The answers to the above questions lie in the fact that no one country is self-sufficient with all resources. Hence, there is the need to engage in trade with other countries to procure goods and services which are in deficiency in the home country and to find market for its indigenously manufactured goods. Adam Smith proposed the theory of absolute advantage that says that international trade takes place because one country may be more efficient in producing a particular good than another country, and that other country may be capable of producing some other good more efficiently than the first one. This provides an incentive to trade as both the countries can benefit from specialization and the resultant increase in productivity. David Ricardo's theory of comparative advantage states that as two countries trade, it will stimulate demand in the domestic market too and improve the profitability of domestic firms. The International trade of any country is divided into two types of trade: Exports: Exporting goods or services to overseas countries requires adherence to several regulatory guidelines and procedural formalities. In India, the Government of India announces Export Import Trade Policy every year and time to time come out with mid-term corrections as and when required. The government also facilitates various incentives to exporters in various modes. Imports: The import of goods refers to purchase of goods or services from other countries within the framework of Export Import Policy. 14.6.1 Regulations for International Trade in India The regulatory framework for International Trade in India comprises of the following: Foreign Exchange Management Act—This Act was formulated in 1999 and replaced the erstwhile FERA (Foreign Exchange Regulation Act). The Act liberalized the exchange controls on foreign investment. Under FEMA, the emphasis is on management of foreign exchange resources. It brought clear

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distinction between current account and capital account transactions. The distinction is summarized as follows: ? All current account transactions are permitted unless otherwise prohibited ? All capital account transactions are prohibited unless otherwise permitted

Main Features of Foreign Exchange Management Act, 1999 The main features of FEMA, 1999 are as follows: 1. FEMA classifies transactions into capital account and current account transactions. 2. Capital account transaction is defined as one that alters the assets or liabilities including contingent liabilities, outside India of persons resident in India, or, assets and liabilities in India of persons resident outside India. Capital account transactions are classified into prohibited capital account transactions and permissible capital account transactions. 3. A Current account transaction is defined as one that is not capital in nature and includes payments due in connection with foreign trade, other current business services and short-term banking and credit facilities in the ordinary course of business. It is further classified into banned transactions, transactions requiring approval from appropriate authorities and transactions permitted within prescribed limits. 4. Full freedom is given to a person resident in India who was earlier outside India to hold or transfer any foreign security or immovable property situated outside India and acquired when he/she was a resident there. 5. A person resident outside India is also permitted to hold shares, securities and properties acquired while he/she was

a resident in India. 6. It has placed more responsibility of Authorised Dealers who have to prescribe the documentation for current account transactions and have to keep them safe till verification by RBI. 7. Proceeds of exports have to be brought in within 180 days but the reference to the date has been deleted. 8. The limit for permitting overdraft in Non-Resident Operation accounts has been dispensed with. Authorized Dealers may permit overdraft in such accounts as per their discretion. Foreign Trade Policy/Exim Policy — It is a set of guidelines and instructions issued by the Directorate General of Foreign Trade (DGFT) regarding export and import trade in India. The general objectives of this policy are control of import of non-essential items and export promotion. The Foreign trade policy of 2015-20 is currently in operation which is explained in detail in the subsequent sections.

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FEDAI (

Foreign Exchange Dealers Association of India) 22

89%

MATCHING BLOCK 163/173

SA

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Foreign Exchange Dealers Association of India (FEDAI) was set up in 1958 as an association of banks dealing in foreign exchange in India (typically called Authorised Dealers —ADs) as a self-regulatory body and is incorporated under Section 25 of The Companies Act, 1956. Its major activities include framing of rules governing the conduct of inter-bank foreign exchange business among banks vis-à-vis public and liaison with RBI for reforms and development of forex market. Presently some of the functions are as follows: ? Prepare guidelines and rules for forex business ? Train bank personnel in the areas of foreign exchange business ? Provide accreditation to forex brokers ? Advise/assist member banks in settling issues/matters in their dealings ? Represent member banks on government/Reserve Bank of India/other bodies ? Announce daily and periodical rates to member banks

70%

MATCHING BLOCK 157/173

W

are as follows: ? Prepare guidelines and rules for forex business ? Train bank personnel in the areas of foreign exchange business ? Provide accreditation

73%

MATCHING BLOCK 158/173

W

forex brokers ? Advise/assist member banks in settling issues/matters in their dealings ? Represent member banks on government/Reserve Bank of India/other bodies ? Announce daily and periodical rates to member banks

Due to continuing integration of the global financial markets and increased pace of de-regulation, the role of self-regulatory organizations like FEDAI has also transformed. In such an environment, FEDAI plays a catalytic role for smooth functioning of the markets through closer co-ordination with the

71%**MATCHING BLOCK 160/173****W**

RBI, other organizations like FIMMDA, the Forex Association of India and various market participants.

FEDAI also maximizes the benefits derived from synergies of member banks through innovation in areas like new customized products, bench marking against international standards on accounting, market practices, risk management systems, etc. Under the FEMA Act, authorized dealers have been classified into four categories: Category – I: Comprises commercial banks, State Co-operative banks and Urban Co-operative banks. They are permitted to transact in all current and capital account transactions, according to RBI directions issued from time-to-time. Category – II: Comprises upgraded FFCs, Co-operative banks, Regional Rural Banks, and others. They can deal with specified non-trade related current account transactions and also all the activities permitted to Full-Fledged Money Changers. Category – III: Select financial and other institutions. They are allowed to deal in transactions incidental to the foreign exchange activities undertaken by these institutions. 22

Profile of FEDAI: Source: <http://www.fedai.org.in/>

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Category – IV: Full-Fledged Money Changers (FFMC) comprising Department of Posts, Urban Co-operative Banks and other FFCs. They are allowed to deal only in purchase of foreign exchange and sale for private and business visits abroad. 14.6.2 Procedural Guidelines for International Trade in India A person involved in export or import transactions should adhere to the following pre-requisites: Obtaining Import Export Code Compliance with export regulations in India begins with obtaining an export license. To obtain such a license, the exporter should fulfill two pre-requisites —opening a bank account with a bank authorized by RBI and obtaining Import Export Code (IEC) number from the Directorate General of Foreign Trade (DGFT). It is also obligatory for the exporter to get himself registered with an appropriate export promotion council. Registering with Export Credit and Guarantee Corporation (ECGC) is also helpful to avoid risks of non-payment. Uniform Customs and Practice for Documentary Credits (UCPDC) Documentary credit or letter of credit plays a significant role in settling payments occurring in the course of international trade. The International Chamber of Commerce (ICC) has issued certain

93%**MATCHING BLOCK 161/173****W**

guidelines in the name of Uniform Customs and Practice for Documentary Credits (UCPDC) to provide uniform interpretation of terminology used under documentary credit.

The latest version of the rules that govern L/C transactions worldwide is UCP600 effective since 1 July 2007. First uniform rules were published by ICC in 1933. Subsequently, the latest revision was in 2006. Rules for Collection of Bills The International Chamber of Commerce, in keeping with the ICC policy of staying abreast of changes in international commerce, initiated a revision of Uniform Rules for Collections in March 1993. The revised rules, which come into effect on 1 January 1996, replace the Uniform Rules for Collections, the URC 522 of 1993. 14.6.3 Export Trade Procedure The export trade procedure involves the following steps: Pre-Shipment Finance Any advance or loan or any credit extended to exporters by a bank either in domestic or foreign currency for the purpose of manufacturing, procuring, processing or packing of goods before shipment can be called as pre-shipment finance. Pre-shipment finance is also given as working capital expenses towards services on the basis of L/C (Letter of Credit) in favor of exporter or in favor of some other person by overseas buyer or on his behalf by any other person with sufficient evidence of expenses.

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Normally, the period of pre-shipment finance is determined by the bank based on the circumstances of individual case. Each exporter requires pre-shipment finance based on the nature of business such as time for procuring export goods, processing or manufacturing and shipping. The bank may release pre-shipment finance either in lump sum or in stages based on the requirements of the exporter with satisfaction by bank against execution of export order. The bank maintains a separate account for packing credit/pre-shipment finance to monitor the period of sanction of such pre-shipment loan and end use of amount. As per the RBI guidelines, exporters are required to submit export documents with the bank after export takes place. If pre-shipment advances are not adjusted by submission of export documents within 360 days from the date of advance, the advances will cease to qualify for the prescribed rate of interest for export credit to the exporter. The commercial interest rate is charged from the date of disbursement of pre-shipment finance. Refinance is provided by RBI for a maximum period of 180 days with permission. Types of Pre-Shipment Finance Pre-Shipment credit can take the following forms: a. Packing credit: Requirement for getting packing credit facility is provided to an exporter who satisfies the following criteria: ? A ten digit importer exporter code number (IEC Number) allotted by DGFT. ? Exporter should not be in the caution list of RBI. ? If the goods to be exported are not under OGL (Open General License), the exporter should have the required license/quota permit to export the goods. The confirmed order received from the overseas buyer should reveal the information about the full name and address of the overseas buyer, description, quantity and value of goods (FOB or CIF), destination port, and the last date of payment. b. Advance against cheques/draft representing advance payments: Where exporters receive direct payments from abroad by means of cheques/drafts, etc., the bank may grant export credit at concessional rates to the exporters of goods based on track record, till the time of realization of the cheque or draft proceeds are received. The banks, however, must satisfy themselves that the proceeds are against an export order. Eligibility for Pre-Shipment Finance Pre-shipment credit is only issued to that exporter who has the export order in his own name. However, as an exception, financial institutions can also grant credit to a third party manufacturer or supplier of goods who does not have export orders in their own name. In such a case, some of the responsibilities of

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meeting the export requirements have been outsourced to them by the manufacturing exporter. In other cases, where the export order is divided between two or more than two exporters, pre-shipment credit can be shared between them. Quantum of Finance The finance is granted to an exporter against the L/C or an expected order. The only guiding principle is the concept of need based finance. To ensure that exporters have their skin in the game, banks impose margins on them depending on factors such as: ? The nature of export order ? The nature of the commodity ? The capability of exporter to bring in the requisite contribution ? Pre-shipment Credit in Foreign Currency (PCFC) Liquidation of Credit PCFC can be liquidated from the proceeds of export documents after their submission for discounting/rediscouting under the EBR Scheme or by the grant of foreign currency loans (DP bills) subjected to the mutual agreement between the exporters and the bankers. This can also be repaid/or prepaid out of balances in Exchange Earners' Foreign Currency A/C (EEFC A/C), or from rupee resources of the exporter to the extent exports have really taken place. Rates of Interest In 1967, RBI introduced export financing for the first time to provide short-term working capital facility at internationally competitive rates. Based on the recommendations of Deepak Mohanty Committee, banks were advised to switch over to a system of base rate w.e.f 1 July 2010. Banks are permitted to fix the rates of interest with reference to ruling LIBOR or EURO LIBOR or EURIBOR. For example, the interest rates as shown in

Exhibit 14.1 were applicable to the exporter clients of SBI in 2021: Exhibit 14.1: Interest Rates on Pre-Shipment Credit and Export Bill Discounting in Foreign Currency Loans Type of Credit and Interest Rate Slabs Interest Rates A. Pre-Shipment Credit in Foreign Currency (PCFC) i) Up to 90 days 3 months LIBOR/EUROLIBOR/EURIBOR+ 2.00% ii) Beyond 90 days & up to 180 days 6 months LIBOR/EUROLIBOR/EURIBOR+ 2.00%

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iii) Beyond 180 days and up to 360 days Rate for initial period of 180 days prevailing at the time of extension plus 2.00%. iv) If no export takes place within 360 days PCFC to be adjusted immediately by sale of foreign currency against rupees at prevailing TT selling rate. Interest to be recovered at 2% over the rate applicable to the cash credit a/c of borrower from the date of advance. Interest recovered earlier at LIBOR related rates to be adjusted. B. Export Bills Rediscounting Scheme (EBR) i) On demand bills for transit period (as specified by FEDAI) 1 month LIBOR/EURO LIBOR/EURIBOR + 2.00% ii) Usance bills (for total period comprising usance period of export bills, transit period as specified by FEDAI and grace period wherever applicable) up to 3 months from the date of shipment 3 months LIBOR/EURO LIBOR/EURIBOR + 2.00% iii) Usance bills (for total period comprising usance period of export bills, transit period as specified by FEDAI and grace period wherever applicable) beyond 3 months up to 6 months from the date of shipment 6 months LIBOR/EURO LIBOR/EURIBOR + 2.00% iv) Export Bills (demand and usance) realized after due date but up to date of crystallization. Rate for B(ii) /B(iii) above plus 2.00% Source: www.sbi.co.

in, 2021 Advances against Claims of Duty Drawback Pre-shipment finance is also provided against duty drawback entitlements that are provisionally certified by the customs. These loans will be adjusted when the final assessment is done by the customs which subsequently refunds the duties. Banks usually grant duty drawback loans towards post-shipment stage for a period of 90 days at lower interest rates. Role of Customs and C&F Agents Services such as loading and unloading of goods, booking of space, customs clearance, etc., are provided by the freight forwarders on behalf of exporters and as such their earnings include commissions paid towards these services. Customs Formalities The exporter must submit certain documents such as shipping bill in case of export by sea or air and bill of export in case of export by road in order to

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receive customs clearance. The following are the different kinds of shipping bills: ? White shipping bill prepared in triplicate to be submitted for export of duty free goods. ? Green shipping bill prepared in quadruplicate to be submitted for export of goods under which duty drawback is to be claimed. ? Yellow shipping bill in triplicate to be submitted for export of dutiable goods. ? Blue shipping bill prepared in seven copies required for exports under the DEPB (Duty Entitlement Pass Book) scheme. ? Other documents necessary for processing a shipping bill are GR forms, AR4 invoice, inspection certificate, and purchase order of the buyer, etc. Initially, the customs appraiser checks the quantity and value of goods in the shipping bill with that mentioned in the L/C or purchase order. He also checks whether the formalities such as exchange control regulations, pre- shipment inspection, etc., have been complied with or not. On completion of verification, all the documents excluding the original GR form, the original shipping bill and a copy of the commercial invoice are given to the forwarding agent to be submitted to the dock appraiser. The customs department submits the original GR form to the RBI. The dock appraiser endorses on the duplicate copy of the shipping bill "Let Export". The documents are then returned to the forwarding agent who in turn submits them to the preventive officer of the customs department. The customs officer endorses on the duplicate copy of the shipping bill "Let Ship". The forwarding agent hands over this duplicate copy to the agent of the shipping company. Subsequently, the captain of the ship carrying the goods gives a "Mate Receipt" to the Shed Superintendent of the port. The mate receipt is given to the forwarding agent after the payment of port charges. When the mate receipt is shown to the preventing officer, he records the certificate of the shipment on all the copies of the shipping bill, original and duplicate copies of the AR4. Finally, the mate receipt is submitted by the forwarding agent to the shipping company to obtain the bill of lading. The exporter, after shipping the goods, must send a shipping advice to the importer along with major documents such as non-negotiable copy of bill of lading, invoice, etc. Incentives Available to the Exporters In order to obtain foreign exchange and promote exports, the Government of India has rolled out various schemes which provide the following incentives and benefits:

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and Finance 209 Free Trade Zones (FTZ): Companies manufacturing goods for export purposes operating from FTZs need not pay excise duties. Further, goods being brought into these zones from different parts of the country are brought without the payment of any excise duty. Moreover, no customs duties are payable on imported raw material and components used in the manufacture of such goods being exported. If entire production is not sold outside the country, the unit has the provision of selling 25% of their production in India. On such sale, the excise duty is payable at 50% of basic plus additional customs or normal excise duty payable if the goods were produced elsewhere in India, whichever is higher. Electronic Hardware Technology Park/Software Technology Parks: This scheme is similar to FTZ scheme; however, it is restricted to units in the electronics and computer hardware and software sector. Special Economic Zones (SEZs): The Special Economic Zone (SEZ) policy in India first came into inception on 1 April 2000. The prime objective was to enhance foreign investment and provide an internationally competitive and hassle free environment for exports. The idea was promoting exports from the country and realizing the need that level playing field must be made available to the domestic enterprises and manufacturers to be competitive globally. SEZ is a geographical region that has economic laws different from a country's typical economic laws. Usually, the goal is to increase foreign investments. SEZs have been established in several countries including China, India, Jordan, Poland, Kazakhstan, Philippines, and Russia. North Korea has also attempted this to a degree. At present there are nine SEZs located at Santa Cruz (Maharashtra), Cochin (Kerala), Kandla and Surat (Gujarat), Chennai (Tamil Nadu), Visakhapatnam (Andhra Pradesh), Falta (West Bengal), Noida (Uttar Pradesh), and Indore (Madhya Pradesh). Exhibit 14.2 gives an overview of SriCity, an integrated business city Exhibit 14.2: Sri City – An example of an Integrated Business City Sri City is an ambitious project of the Andhra Pradesh Government which is located 55 kms north of Chennai and serves in inter-linking both the states of Andhra Pradesh and Tamil Nadu. It is spread over 100 sq.km and is designed with the state-of-the-art eco-friendly infrastructure. The city provides a hub that houses a Special Economic Zone (SEZ) for export oriented units, a Domestic Tariff Zone (DTZ) for businesses catering to the domestic markets and a Free Trade and Warehousing Zone (FTWZ). It also has a live zone that has residential, recreational, health care and other facilities. The city provides ready to occupy factories for customers who want to begin operations immediately. For those customers who want more specific infrastructure, the city offers built to suit option.

Source: www.sricity.in

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Export Oriented Units (EOU): In the early 1980s, EOU concept was introduced to boost exports by creating additional production capacity. The scheme has witnessed significant changes in the past three decades and is complementary to the Export Processing Zone (EPZ) scheme, except that it is widely spread unlike EPZs which are set up at specific locations. EOUs can be set up for manufacturing goods, including repairing, remaking, reconditioning, re-engineering and rendering of services. Almost 100% EOUs fall into three categories, viz.: a. EOUs established anywhere in India and exporting 100% products except certain fixed percentage of sales in the Domestic Tariff Area (DTA) as may be permissible under the policy b. Units in Free Trade Zones in Special Economic Zones (SEZs) and exporting 100% of their products c. EOUs set up in Software Technology Parks (STPs) and Electronic Hardware Technology Parks (EHTPs) of India for development of software & electronic hardware. Advance Licence/Duty Exemption Entitlement Scheme (DEEC): Advance licence which can be either quantity-based (Qbal) or value-based (Vabal), is given under this scheme to an exporter against which the raw materials and other components may be imported without payment of customs duty provided the manufactured goods are exported. These licences are transferable in the open market at a price. Export Promotion Capital Goods Scheme (EPCG): A domestic manufacturer can import plant and machinery without paying customs duty or settling at a concessional rate of customs duty.

But his undertakings should be as mentioned below in Exhibit 14.3: Exhibit 14.3: Customs Duty Rate on Export Obligations Customs Duty Rate Export Obligation Time 10% 4 times exports (on FOB basis) of CIF value of machinery 5 years Nil in case CIF value is ` . 20 crore or more 6 times exports (on FOB basis) of CIF value of machinery or 5 times exports (on NFE basis) of CIF value of machinery 8 years Nil in case CIF value is ` 5 crore or more for agriculture, aquaculture, animal husbandry, floriculture, horticulture, poultry, and sericulture 6 times exports (on FOB basis) of CIF value of machinery or 5 times exports (on NFE basis) of CIF value of machinery 8 years (FOB - Free On Board; CIF - Cost, Insurance & Freight; NFE - Net Foreign Exchange) Source: www.indianindustry.com, 2015 Unit 14: Basics of International Trade and Finance 211

Deemed Exports: The Indian suppliers are entitled for the following benefits in respect of deemed exports: ? Refund of excise duty paid on final products ? Duty drawback ? Imports under DEEC scheme ? Special import licences based on value of deemed exports Manufacture under Bond: In this scheme, manufacturers execute a bond of adequate amount to assume export obligation. On the strength of this bond, the manufacturer is allowed to import goods without paying any customs duty or source it locally without paying excise duty. The production is made under the supervision of customs or excise authority Duty Drawback: It means the rebate of duty chargeable on imported material or excisable material used in the manufacturing of goods that is to be exported. The exporter may claim drawback or refund of excise and customs duties being paid by his suppliers. The final exporter can claim the drawback on material used for the manufacture of export products. In case of re-import of goods, the drawback can be claimed. The following are the drawbacks: ? Customs paid on imported inputs plus excise duty paid on indigenous imports ? Duty paid on packing material Post-Shipment Finance Post-shipment finance is provided to finance export sale receivables of the exporter. It can be defined

40%

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as any loan or advance granted or any other credit provided by an institution to an exporter from India. This form of finance is provided from the date of extending the credit after shipment of goods to the date of realization of the export proceeds. Different types of post-shipment finance

are as follows: 1. Export bills purchased/discounted 2. Export bills negotiated 3. Advance against export bills sent on collection basis 4. Advance against export on consignment basis 5. Advance against undrawn balance on exports 6. Advance against claims of duty drawback Eligibility for Post-Shipment Finance

Post-shipment finance is provided to the actual exporter or to an exporter in whose name the export documents are transferred. Finance is also extended to deemed exporters in the case of deemed exports. In case of cash exports, the exporter must submit documents such as GR form, PP form, etc., along with shipping documents for negotiation.

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Quantum Post-shipment finance can be extended up to 100% of the invoice value of goods. In special cases, where the domestic value of the goods increases the value of the exporter order, finance for a price difference can also be extended and the price difference is covered by the government. However, this type of finance is not extended in case of pre-shipment stage. Banks can also finance undrawn balance. In such cases, banks are free to stipulate margin requirements as per their usual lending norm. Period of Finance and Interest Rates Applicable Post-shipment finance can be either short-term or long-term depending on the payment terms offered by the exporter to the overseas importer. In case of cash exports, the maximum period allowed for realization of exports proceeds is six months from the date of shipment. Concessional rate of interest is available for a highest period of 180 days, opening from the date of surrender of documents. Usually, the documents need to be submitted within 21 days from the date of shipment.

14.6.4 Import Trade Procedure

Under import financing, banks provide financial assistance for activities involving import of plant and machinery, consumable inputs, channelized goods, opening of import letter of credit, issuing deferred payment guarantees, assisting overseas seller in the interest of the importer based on long-term credit. Banks also provide import finance through different modes such as cash credit, loans against import trust receipt and direct payment in foreign exchange to overseas sellers. Pre-requisites for Opening an Import Letter of Credit An importer's appeal to open a letter of credit is carefully examined by a bank with regard to trade control requirements, exchange control requirements, credit norms of RBI, UCPDC 600 (Uniform Customs & Practice for Documentary Credits) provisions, FEDAI (Foreign Exchange Dealers Association of India) and lastly, internal procedures of the bank. A bank in accordance with exchange control guidelines can permit opening of letters of credit by its own customers who are engaged in the trade. To open a letter of credit the importer must submit an application-cum-agreement in the desired form to the bank. He must also attach required documents such as exchange control copy of the import licence, pro-forma invoice, sale contract between importer and exporter, and so on. At the time of submission, the importer must carefully check all the procedural formalities like terms and conditions mentioned, authorized signature at all the required places on the form, validity of contract, etc. On the other hand, to ensure the creditworthiness of the importer, banks secure certain information such as possession of importer exporter code number by the importer, validity of import licence and other information. An import letter of credit should be in compliance with exchange control aspects. For this purpose, the importer should have good knowledge about various exchange control

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aspects. For example, any imports on cash basis remittance should be concluded within six months from the shipment date. When the bank is satisfied from all the aspects, it opens a letter of credit in favor of the supplier of goods. Customs Procedure for Clearance of Imports into India The importer should present an import manifest to the customs department within 24 hours of the goods being dispatched. The manifest must contain information of all the goods that are placed on board of vessel. The importer on receiving the information of advent of goods must file a bill of entry in the desired form with the department of imports under the customs house. Here, the submission date of the bill of entry is of vital importance because the goods will be assessed for duty based on the rate prevailing on the date of submission. After the bill of entry is noted by the imports department, it is submitted at appraising counters along with documents such as import licence, certificate of origin, copy of letter of credit, exporter's invoice, weight specifications, double copy of packing list, customs declaration, etc. The appraiser, after verifying and completing the bill of entry, will get it countersigned by the assistant controller. Then the bill is sent to the licence department with a notification to dock the staff for scrutiny of goods prior to clearance. The appraising procedure for bill of entry may be the first check procedure or second check procedure. In the first check procedure, after the preliminary examination of documents presented, the appraiser returns the bill of entry ordering for scrutiny of goods before the duty is assessed. In the second procedure, after the duty payment, the importer or his representative must acquire the duplicate of bill of entry from the customs department according to which the order for the scrutiny of goods is issued. 14.6.5 General Provisions Governing Exports and Imports Foreign Trade Policy 2015-20 gives a fillip to "Make in India" through import substitution and simultaneously boosts exports to effectively manage the current account deficit. The general provisions concerning imports to and exports from India are governed by the following rules, regulations, procedures, etc., as detailed in the FTP. a. Exports and imports shall be 'Free' except when regulated by way of 'prohibition', 'restriction' or 'exclusive trading through State Trading Enterprises (STEs)' as laid down in Indian Trade Classification (Harmonized System) [ITC (HS)] of Exports & Imports. b. ITC (HS) is a compilation of codes for all merchandise/goods for export/import. Goods are classified based on their group or sub-group at 2/4/6/8 digits. c. Imports should be in compliance with the domestic laws, unless specifically exempted. However, goods to be utilized/consumed in manufacture of export products, as notified by DGFT, may be exempted from domestic standards/quality specifications.

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d. Import Export Code number (IEC) is a 10-digit number allotted to a person that is mandatory for undertaking any export/import activities. Now the facility for IEC in electronic form or e-IEC has also been operationalized. e. Mandatory documents required for export of goods from India: Bill of Lading/Airway Bill, Commercial Invoice cum Packing List, and Shipping Bill/Bill of Export. f. Mandatory documents required for import of goods into India: Bill of Lading/Airway Bill, Commercial Invoice cum Packing List, and Bill of Entry. g. Any goods/service, the export or import of which is 'Restricted' may be exported or imported only in accordance with an Authorization/Permission or in accordance with the procedure prescribed in a Notification/Public Notice issued in this regard. h. SCOMET (Special Chemicals Organisms Materials Equipment Technology) items exported under Defense Offset Export Policy will now go through a simple verification of end user certificate. i. Goods which are importable freely without any 'Restriction' may be imported by any person. However, if such imports require an authorization, actual user alone may import such good(s) unless such a clause is specifically dispensed with by DGFT. j. Country-specific restrictions would be applicable in case of exports and imports related to "arms and related material" while dealing with Iraq. However, an NOC from the Department of Defense Production would allow import or export of the same. Similar prohibitions are also placed on indirect import/export with People's Republic of Korea & Iran. Import of charcoal from Somalia is also prohibited. k. State Trading Enterprises are governmental and non-governmental enterprises, including marketing boards, which deal with goods for export and/or import. Any good, import or export of which is governed through exclusive or special privilege granted to STE, may be imported or exported by the concerned STE as per conditions specified in ITC (HS). l. All goods and services which are exported from units in Domestic Tariff Area (DTA) and units in Export Oriented Units (EOU)/Electronic Hardware Technology Park (EHTP)/Software Technology Park (STP)/Biotechnology Park (BTP), exemption/remission of service tax levied and related to exports, shall be allowed, as per prescribed procedure. m. In case of third party exports (except Deemed Export), export documents such as shipping bills shall indicate the name of both manufacturing exporter/manufacturer and third party exporter(s). Bank Realization Certificate (BRC), export order and invoice should be in the name of third party exporter.

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n. Goods imported may be exported in same or substantially the same form without an authorization provided that item to be imported or exported is not restricted for import or export in ITC (HS). o. All export contracts and invoices shall be denominated either in freely convertible currency or Indian rupees but export proceeds shall be realized in freely convertible currency. p. Authorization to import/export listed as 'Restricted' items in ITC (HS) requires Registration-cum-Membership Certificate (RCMC). Export Promotion Councils (EPCs) are organizations of exporters, set up with the objective to promote and develop exports. EPCs are also eligible to function as Registering Authorities to issue Registration-cum-Membership Certificate (RCMC) to its members. q. Manufacturers who are also

Status Holders (business leaders who have excelled in international trade)

shall be eligible for Approved Exporter Scheme. Approved Exporters

will be entitled to self-certify their manufactured goods as originating from India with a view to qualifying for

preferential treatment. 14.7 Role of EXIM Bank EXIM Bank was set up to finance and promote foreign trade. It extends finance to exporters of capital and manufactured goods, exporters of software and consultancy services and to overseas joint ventures and turnkey/construction projects. Term loans are also extended to projects located in export zones. EXIM Bank financing can, if required, supplement working capital finance extended by commercial banks at pre-shipment stage. The functions of the EXIM Bank are lending, guaranteeing, promotional services, and advisory services.

Table 14.1 details the lending functions of EXIM Bank. Table 14.1: Lending Functions of EXIM Bank Source: ICFAI Research Center

Block IV: Financial Management 216 14.7.1

Lending to Indian Companies The EXIM Bank's lending facilities to Indian Companies comprise of the following types of financial assistance. **Direct Assistance Funds** are provided on deferred payment terms to Indian exporters of plant, equipment and related services, which enable them to extend deferred credit to the overseas buyer. Credit is provided by EXIM Bank in participation with commercial banks. Banks provide the credit and they can avail refinance facility for the credit provided from the EXIM Bank. The exporter is expected to obtain an advance and a down payment of at least 15 percent of the contract value. **Consultancy and Technology Services** Indian companies executing overseas contracts involving consultancy and technology services, can avail EXIM's financing program, to offer deferred payment terms to their clients. The credit may be extended to the Indian company either by the EXIM Bank in participation with commercial banks, or directly by commercial banks who could in turn seek refinance from EXIM Bank. The Indian company in turn would offer deferred payment terms to their clients. The credit normally given in Indian rupees is repayable in half-yearly instalments over a period not exceeding five years. Guarantee of foreign government or a guarantee/irrevocable LC of an acceptable bank would need to be obtained. The Indian company also has to obtain ECGC insurance cover and assign it in favor of the bank. **Overseas Investment Finance** The EXIM Bank provides export credits to Indian promoters for their equity contribution to overseas joint ventures. The funds are in the form of long-term credit not exceeding ten years. EXIM Bank's finance will be made available to Indian promoters by way of: i. Rupee term loans for financing equity contribution. ii. Foreign currency loans/guarantees, where the equity contribution is allowed by the Government of India out of foreign currency loan to be raised by the Indian promoter. Equity contribution by Indian promoters can be in various forms such as: a. Capitalization of proceeds of exports in the form of plant and machinery; b. Technical know-how; c. Capitalization of earnings such as royalty and management fees; and d. Cash remittances

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Where cash remittances are allowed, Indian promoters are granted approvals to remit foreign exchange from India or raise foreign currency loans for the purpose of equity contribution. The quantum of finance will be determined with reference to the Indian promoters' share in the equity structure of overseas joint ventures, subject to a maximum of 80 percent of the Indian promoters' equity contribution. Commercial banks may also opt to take up risk participation in term loans and guarantees extended by EXIM Bank. **Pre-Shipment Credit** If the requirement of pre-shipment credit by exporters is for periods in excess of 180 days, EXIM Bank participates in the credit. **Financing Deemed Exports** Deemed exports occur in case of specified transactions within India, which result in foreign exchange earnings or savings as given below: i. Supplies made in India to World Bank/IDA-aided projects against international competitive bidding. ii. Supplies to free-trade zones/100 percent export-oriented units. iii. Sales to foreign shipping companies. iv. Supplies to ONGC and Oil India Ltd., for offshore and onshore drilling operations. Deemed exports can avail EXIM Bank's deferred credit facility. EXIM Bank may participate with commercial banks in extending rupee loans for bridging cash flow deficits of projects/supply contracts; EXIM Bank also issues guarantees and provides bridge finance in foreign currency. Capital and producer goods are eligible for medium-term credits. Long-term credits up to ten years are provided in exceptional cases. Credit is normally secured by a bank guarantee. **Assistance to Export-Oriented Units** Free-trade zones and export-oriented units are given finance for acquisition of land, building, plant and machinery, preliminary and pre-operative expenses, and working capital (as margin money). EXIM Bank's assistance will be in the form of direct assistance given as rupee term loans or deferred payment guarantees or indirect assistance as refinance to commercial banks. The export-oriented units seeking EXIM's finance will have to establish the technical, economic and financial feasibility of their projects. **Forfeiting** Forfeiting is a common form of financing export-related receivables.

It is similar to Bill Rediscounting Scheme. EXIM Bank has introduced this scheme for the Indian exporters. Under this scheme, the exporter, after finalization of the sale (or contract) with a prospective buyer, furnishes all the necessary details

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regarding the contract to the EXIM Bank, through which a contract of forfaiting is finalized by the exporter with the overseas forfaiting agency. The exporters draw a series of bills of exchange on the overseas buyer which will be sent along with the shipping documents to the buyer's bank for overseas buyer's acceptance. The overseas buyer's bankers will hand over to the exporter the documents against the acceptance of the buyer and signature of 'aval' or the guaranteeing bank. The exporter will submit the documents to his bank to be forwarded to EXIM Bank which passes the documents to the forfaiting agency. Proceeds of the bills are passed from the overseas forfaiting agency to the exporter through the EXIM Bank. Since 1997, authorized dealers are allowed to undertake forfaiting of medium-term export receivables.

Figure 14.1 depicts the flow chart of a forfaiting transaction Figure 14.1: A Flow Chart of a Forfaiting Transaction Source: ICFAI Research Center 1.

Commercial contract between the foreign buyer and the Indian exporter. 2. Commitment to for fait bills of exchange/promissory notes (debt instruments). 3. Delivery of goods by the Indian exporter to the foreign buyer. 4. Delivery of debt instruments. 5. Endorsement of debt instruments without recourse in favor of the for fairer. 6. Cash payment of discounted debt instruments. 7. Presentation of debt instruments on maturity. 8. Payment of debt instruments on maturity.

Unit 14: Basics of International Trade and Finance 219 14.7.2 Lending to Foreign Governments and Foreign Companies The EXIM Bank's lending to Foreign Governments and Foreign Companies comprise of the following types of financial assistance. Buyers' Credit Credit is given to buyers abroad to enable them to import engineering goods from India on deferred payment terms. The loan facility is to be secured by a letter of credit or a bank guarantee. Lines of Credit EXIM Bank also extends lines of credit to overseas governments or agencies nominated by them, to enable buyers in these countries to import capital/engineering goods from India on deferred payment terms. The exporters can obtain payment from EXIM Bank against negotiation of shipping documents. Relending An overseas bank can enter into a credit line agreement with EXIM Bank. The overseas bank would relend the funds to importers of capital goods, consumer durables and services from India. The borrowing bank may be a commercial bank, a central bank, or an investment/merchant bank with a good credit standing. Figure 14.2: Specimen Copy of a

Promissory Note Source: ICFAI Research Center

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Figure 14.3: Specimen Copy of a Bill of Exchange Source: ICFAI Research Center

Loans will be denominated in US dollars and repayment will also be in the same currency. Short-term loans extending from 180 days to one year are repayable by quarterly/half-yearly installments. Medium-term loans are also extended. The relending facility will operate as follows: a. The borrowing bank, upon its approval of a sub-loan to an importer, opens irrevocable letters of credit in favor of the Indian exporter through EXIM Bank or banks designated by the latter. b. The Indian exporter ships goods and presents shipping documents to EXIM Bank or banks designated by the latter. c. EXIM Bank pays to the Indian exporter the rupee equivalent. d. EXIM Bank or the negotiating bank in India forwards shipping documents to the borrowing bank, together with the advice of having made disbursement to the supplier. 14.7.3 Lending to Indian Banks The EXIM Bank's lending to Indian Banks comprise of the following types of financial assistance. Rediscounting of Export Bills Commercial banks that are authorized dealers can rediscount their short-term usance export bills with EXIM Bank.

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Refinance for Deferred Payment Exports Deferred payment exports arise when export proceeds are to be received after six months from the date of shipment. EXIM Bank offers hundred percent refinance facility to banks, which enables a bank to extend deferred credit to an Indian exporter against supplier's credit offered by the exporter to the overseas buyer. Capital goods, consumer durables and industrial manufactures can be considered for deferred credit. Guarantees Guarantees are issued by the EXIM Bank on behalf of exports of turnkey projects and construction contracts. Such guarantees include: i. Bid bond guarantee ii. Advance payment guarantee iii. Performance guarantee iv. Retention money guarantee v. Guarantee for borrowing abroad Bid bond guarantee is issued for a maximum period of six months. For advance payment guarantee, exporters are expected to secure mobilization advance of 10-20 percent of contract value. Performance guarantee for 5 to 10 percent of contract is issued and is valid up to one year after completion of the contract. Guarantee for release of retention money enables the exporter to obtain the release of full payments. Bridge finance may be needed at the earlier phases of the contract. Up to 10 percent of the contract value may be raised in foreign currency from a foreign bank against the EXIM Bank's guarantee for borrowing abroad. Syndication of Export Credit Risks EXIM Bank and other banks participating in the funding of a loan would syndicate the respective credit risks to other eligible commercial banks, who would assume part of the total risk. Proposals valued at more than ` 1 crore, entailing deferred credit exports of engineering goods and services, are forwarded by the sponsoring bank for consideration by an inter-institutional working group which meets at Mumbai, with EXIM Bank as the focal point. While clearing the proposal, the participation arrangement for the funding of export credit is also determined. Software Exports The new policy of the government on computer software exports and development has rationalized the system of facilities and incentives for exports. Under the new policy, EXIM Bank has been designated as an agency for facilitating speedy clearances and meeting foreign exchange requirements towards imports for computer software export where export obligation of 350

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percent of foreign exchange used is undertaken. EXIM Bank will undertake financial and technical analysis of software export proposals and monitor the progress. EXIM Bank extends advisory services to exporters in several areas and undertakes promotional activities like techno-economic surveys collecting and disseminating market information. EXIM Bank offers an integrated package covering foreign currency and rupee term finance for acquisition of imported and indigenous computer/computer- based systems for export purposes. EXIM Bank welcomes the association of commercial banks for providing working capital finance for software export projects assisted by it. A rebate of 50 percent on customs duty payable on import of computer system is available to software exporters opting for 350 percent export obligation. Export and import transactions are governed by the EXIM policy and the RBI exchange control regulations. While the EXIM policy regulates the movements of goods and services by prescribing the permissible exports and imports, the RBI regulations regulate the corresponding payments for these international transactions. While extending credit for any such trade, the banks need to make sure that the respective guidelines have been followed by the concerned parties.

14.8 Exchange Control Regulations - FEMA Exchange controls were introduced in India in 1939, during the World War II, to conserve foreign exchange, particularly the US dollar, for meeting essential defence expenditure. The main purpose of exchange controls is to conserve foreign exchange and ensure its effective utilization. After the World War II, the exchange control regulations framed under the Defence of India Rules were replaced by the Foreign Exchange Regulation Act, 1947, which was revised and replaced by the Foreign Exchange Regulation Act, 1973. With a view to create conducive climate for attracting foreign direct investment to increase production and promote exports, FERA 1973 has been substantially amended by FERA [Amendment] Act, 1993. FERA was replaced with Foreign Exchange Management Act (FEMA), 1999 to consolidate

81%	MATCHING BLOCK 166/173	SA	FMG-302 Indian Financial System and Management ... (D164737022)
and amend the law relating to foreign exchange with the objective of facilitating external trade and payments and for promoting the orderly development and			
100%	MATCHING BLOCK 164/173	W	
orderly development and maintenance of foreign exchange market in India.			
100%	MATCHING BLOCK 165/173	W	
orderly development and maintenance of foreign exchange market in India.			
100%	MATCHING BLOCK 168/173	SA	mangal . Intoduction to Financial Markets & In ... (D22478819)
orderly development and maintenance of foreign exchange market in India.			

Exchange controls also cover foreign capital and activities financed by it. The administrative authority of foreign exchange regulation is vested with the Reserve Bank of India (RBI) and the routine work of exchange control is delegated to banks authorized to deal in foreign exchange. Exchange controls and procedures are set out in the Exchange Control Manual published by the RBI.

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Transactions Subject to Control The transactions that are regulated under the Exchange Control Manual published by the RBI are as follows: a. Purchase, sale, and other dealings in foreign exchange and maintenance of balance at foreign centers. b. Realization of export proceeds and payment for imports. c. Payments to non-residents or to their accounts in India. d. Transfer of securities between residents and non-residents and acquisition and holding of foreign securities. e. Foreign travel with foreign exchange. f. Export and import of currency, cheques, travelers' cheques, securities, etc. g. Activities in India of foreign nationals and branches of foreign firms and companies. h. Foreign direct investment and portfolio investment in India including investment by non-resident Indians, persons of Indian origin and corporate bodies predominantly owned by such persons. i. Appointment of non-residents and foreign nationals and foreign companies, etc., as agents in India. j. Setting up of joint ventures/subsidiaries outside India by Indian companies. k. Acquisition, holding and disposal of immovable property in India by foreign nationals/companies.

14.9 Highlights of Foreign Trade Policy The government of India released the new five year Foreign Trade Policy for 2015 to 2020 in April, 2015. This policy provides a framework for increasing exports of goods and services as well as generation of employment and increasing value addition in the country. The main objectives of this policy are: ? To increase India's share in world exports from 2% to 3.5% by 2020. ? To provide a stable and sustained policy environment for export of merchandise and services. ? To connect varied policies, procedures and guidelines of foreign trade with other major initiatives such as "Make in India", "Digital India" and "Skill India" to create "Export Promotion Mission" for India. ? To widen export product basket by identifying new sectors that have potential. ? To provide a mechanism for regular appraisal for rationalizing imports and reducing trade imbalance.

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Foreign Trade Policy (2015-20) aims at enhancing the country's exports and use trade expansion as an effective instrument of economic growth and employment generation. Key highlights of this policy are: a. Merchandise Exports from India Scheme (MEIS) The MEIS scheme is introduced to offset infrastructural inefficiencies and the costs associated with exporting goods produced in India. The main features of this scheme are: ? Existing multiple schemes such as Focus Product Scheme, Market Linked Focus Product Scheme, Focus Market Scheme, Agriculture Infrastructure Incentive Scrip, and Vishesh Krishi Gramin Upaj Yojana have been merged into MEIS. ? Notified goods exported to notified markets/countries would be eligible for benefits ranging from 2-5% of FOB value of exports or FOB value realized, whichever is less. ? The import duty mentioned in the scrip need not be paid by the exporter. This import duty amount would be given as a percentage of the export value made by the exporter. ? The MEIS envisaged higher support for both agricultural and village industry products. These products were to be supported across the globe at rates of 3% and 5% respectively. Processed and packaged agricultural and food items under MEIS will get higher benefits. ? There will be higher levels of support for selected category of products that include: o Agricultural and Village industry products – that were currently covered under Vishesh Krishi Gramin Upaj Yojna (VKGUY) o Value added and packaged products o Eco-friendly and green products o Labor intensive products o Industrial products from potential winning sectors o Hi-tech products with high export earning potential ? Export of goods (FOB value up to INR 25,000), through courier or foreign post office using e-commerce, is also eligible for benefits. ? MEIS scrip can also be used for payment of custom duty, excise duty and service tax. ? Basic/additional custom duty, excise duty and service tax paid through cash or debit to scrip is available for credit to CENVAT (Central Value Added Tax) or drawback.

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Scrip and goods imported/locally procured against the scrip are freely transferable. ? MEIS benefits extended to SEZ units except Free Trade and Warehousing Zone units. ? Exports until 31 March, 2015 and scrips applied for or issued against them will be governed by rules of the earlier relevant schemes. ? In major products, industrial products to be supported at rates ranging from 2% to 3%. ? Defence and technology-oriented products were given further incentives under the MEIS scheme. ? Classification of countries for focus market scheme: Under the new FTP 2015, the focus market scheme has been restructured. Different categories would be provided with incentives based upon their relative importance of the export market potential.

- o
- Category A: Traditional Markets (30) - European Union (28), USA, Canada.
- o Category B: Emerging & Focus Markets (139), Africa (55), Latin America and Mexico (45), CIS countries (12), Turkey and West Asian countries (13), ASEAN countries (10), Japan, South Korea, China, Taiwan,
- o Category C: Other Markets (70).
- b.

83%	MATCHING BLOCK 167/173	W
Service Exports from India Scheme (SEIS) Service Exports from India Scheme is		

a scheme introduced as a modification to the served from India scheme prevalent under the Foreign Trade Policy 2009-14. ? Served from India Scheme is replaced by SEIS. However, all benefits duty exempted scrip of the previous scheme will be extended to service providers located in India and exporting notified services in a specified mode. ? Eligibility of such benefits to service providers requires minimum net foreign exchange earnings of \$15,000 in the preceding financial year. ? Service providers will be issued SEIS scrip of 3% or 5% of net foreign exchange earned depending on the type of service. ? Benefits of SEIS like MEIS are extended to SEZ units also. SEIS benefits are similar to MEIS (including availment of CENVAT credit and drawback). These scrips and the goods imported or locally procured can be freely transferred. ? Exports until 31 March 2015 and scrips applied for or issued against them will be governed by rules of SFIS.

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c.

Export Promotion Capital Goods (EPCG) Scheme This scheme is meant for import of capital goods for pre-production, production and post-production subject to an export obligation. The features of this scheme are: ? Capital goods import under EPCG scheme carries six times export obligation of the duty saved. Reduced export obligation up to 25% has now been prescribed for domestic sourcing of capital goods. ? Exporters registered with the excise authorities subject to conditions now have the option to furnish installation certificate confirming receipt of capital goods by a Certified Engineer. ? Normally, installation certificate is to be furnished within six months of the completion of imports. However, licensing authority can now extend the period of submitting the installation certificate by another 12 months. ? In case of exit of an EOU or SEZ unit under the EPCG scheme, guidelines for maintenance of average export obligation and specified export obligation are notified. d. Export Oriented Unit (EOU)/Software Technology Park (STP) Scheme This scheme which was introduced to encourage exports and software technology parks has the following features: ? Board of Approval (BoA) may grant one year extension for achieving net foreign exchange earnings under special circumstances on a case to case basis. ? Letter of Permission (LoP) will now have initial validity of two years (earlier three years) for implementation of project and commencement of production. Extension of one year (earlier three years) may be considered on a case to case basis. ? Unit sharing of infrastructural facilities between EOUs/STPs may be permitted by Approval Committee (UAC)/Inter Ministerial Standing Committee (IMSC) on a case to case basis or on recommendations of BoA. However, such sharing is not permitted between EOUs/STPs and SEZs. ? STP unit can set up for undertaking repairing, re-conditioning, remaking, testing, etc., for exports subject to the approval of IMSC and other conditions. ? Procedures simplified for fast track debonding/exiting of STP units which have not availed duty exemption benefits. ? Facility to set up a warehouse outside the premises and near a port of export permitted subject to conditions. ? Fast track clearances on procurement are allowed to EOUs having a physical export turnover of ` 10 crore and above.

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e.

Others In addition to the above mentioned schemes, the Foreign Trade Policy of 2015-2020 also outlines the following other schemes: ? Duty Free Import Authorization Scheme which exempted all customs duty is now restricted to only basic custom duty. However, on certain conditions, additional customs duty will be available as CENVAT credit. ? Eligibility criteria for grant of 'status' to an exporter is revised. Deemed export will now be considered for 'export performance'. Self- certification, export promotion, etc., are extended as additional facilitation. ? Advance Authorization Scheme which earlier provided 18 months for export obligation period for exports of defence, military stores, aerospace, COMET items, etc., has now been stretched to 24 months. ? Recovery and penal proceedings in case of mis-declaration and misrepresentation of facts to claim deemed export benefits notified. ? Measures were introduced to facilitate trade for slashing transaction costs and crashing documentation handling time in terms of on-line application filing, on-line inter-ministerial consultation, physical record maintenance, submission of multiple documents, etc. ?

Nomenclature of Export House, Star Export House, Trading House, Premier Trading House certificate changed to 1,2,3,4,5 Star Export House. ?

Status holders (entities/persons who promote substantial export turnover or identified group who help export promotion) were encouraged with specific promotional measures such as:

- o Business leaders who excelled in international trade and contributed successfully to country's foreign trade were recognized as Status Holders and given special treatment and privileges.

o

The nomenclature of Export House, Star Export House, Trading House, Star Trading House, Premier Trading House certificate has been changed to One, Two, Three, Four, Five Star Export House.

o

The criteria for export performance for recognition of status holder were changed from Rupees to US dollar earnings. ?

Structure of Star Trading Houses Status Category Export Performance During current and Previous two years in (USD mn)

100%

MATCHING BLOCK 169/173

SA

JSNR_SSOU_BBA_Global Banking & Finance_Final_T ...
(D27249834)

One Star Export House 3 Two Star Export House 25 Three Star Export House 100 Four Star Export House 500 Five Star Export House 2000

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From Jan, 2021 to July, 2021, Indian exports clocked year-on-year growth of 47.29% with exports amounting to \$ 221,403 Million. For the same period, imports had a year on year growth of 51.19% amounting to \$ 303,763 Million. The top 5 export commodities were – Petroleum products, Pearls, precious stones and semi-precious stones; Iron and Steel; Drug Formulations and Organic Chemicals The top 5 import commodities included Crude petroleum; gold; petroleum products; pearls, precious stones and semi-precious stones; coal and coke. While USA was the top exporting country; China was the top importing country The yearly trend of exports and imports showed that in 2020 both exports and imports declined due to the pandemic impact. When it comes to services exports India registered a year on year decline of 3.33% while imports showed a decline of 8.38 percent The yearly trend of service exports showed a sharp decline from \$ 2,06,090 Million in 2019 to \$ 54,630 Million in 2020. The imports declined from \$117,524 Million in 2019 to \$31,276 Million in 2020

Enhanced Support under MEIS To give a fillip to the exporters, the Department of Commerce has provided under the Merchandise Exports from India Scheme (MEIS), extended support to certain new category of products and also enhanced the incentive rate for certain other specified products. The following are the major highlights of the support implemented through DGFT public Notice No 32 dated 22 September 2016: - Addition of new products: Around 2,901 products falling under varied categories were included from the following areas: ? Traditional medicines such as Ashwagandha herbs and its extracts, other herbs, extracts of different items. ? Marine products, sea feed items. ? Onion dried, processed cereal products and other value added items of plastics, leather articles, suitcases etc. ? Industrial products that fall under varied categories that include ceramics, chemicals, engineering goods, fabrics, garments, glass products, leather goods, made ups, newspapers, periodicals, pipes, silk items, tubes, wool products etc. Increase in MEIS rates: The rates applicable for around 575 product items falling under 11 different products categories have been enhanced. These products cover:

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Iron and steel, handicrafts, moulded and extruded goods, rubber, ceramic, glass, auto tyres and tubes, industrial machinery engineering items, IC Engines, machine tools/parts, items of wood, paper, stationery, footwear, steel furniture, prefabs, items under the category of butter, ghee and cheese, dried egg albumin and rubber products. With this announcement, the aggregate number of items covered under the MEIS scheme shot up from 5012 to 7103. The aggregate financial support extended by Government of India under this scheme shot up from ` 22,000 crore to ` 23,500 crore per annum. Expert Views on Foreign Trade Policy 2015-2020 The focus on FTP has been "Simplicity and Stability" as the policy on the one hand sought to realign the multiple schemes with the objective of reducing complexities. On the other hand, it wanted to promote the increased use of technology to mitigate the transaction cost and manual compliances. Supporters had stated that it was a 'progressive', 'path-breaking' and 'development-friendly' policy as exports of books, handicraft, handlooms, toys, textiles, defence, and e-commerce platforms would be easier and faster. According to these people, a giant step was cleaning up the plethora of export promotion schemes and clubbing them under two schemes, one for goods MEIS and the other for SEIS. The duty scrips under these schemes come without any conditions and were transferable freely. One major announcement in this policy was that it would move away from relying largely on subsidies and sops. However, critics pointed out that, this is prompted by WTO requirements that export promotion subsidies should be phased out. Expert opinion was divided as there are other ways of getting around it, which countries explored always. For many years, boosting services exports had been a talking point. However, information technology and information technology-enabled services (IT/ITES) dominated the export basket to the tune of 50% generally and 90 % in the services export basket exclusively. ITES was overly dependent on western markets and, consequently, extremely vulnerable to minor developments in these markets. This FTP on a positive note had shifted its attention to other sectors that have great export potential – healthcare, education, R&D, logistics, professional services, entertainment, services incidental to manufacturing. By extending the benefits under EPCG on domestic procurements and offering them more products under MEIS, the policy further seeks to incentivize the exports. This is a step in the right direction. It's a focused policy, one in which exports through Make in India is underlined by looking at sectors that give greater employment and have high-tech value

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addition. The object was to join the global value chain and above all, the environment part, where you are looking at eco-friendly systems and producing wealth out of waste. So, the priority areas are technology-driven, labour- intensive-driven, and environment-driven. In addition to it, it is important to look at traditional markets, emerging markets and the markets diversifying into new markets. The FTP 2015-20 was to end and a new FTP 2021-26 was to be implemented from 2021. However, the pandemic impacted the beginning of this FTP. In this scenario, exhibit below captures that

expectations of the trading community towards the new FTP. Exhibit 14.4: Expectations from the Proposed New Trade Policy The Foreign Trade Policy 2015-20 was to be replaced by the new foreign trade policy 2021-26. The big question therefore is whether the new policy will continue with or discontinue the schemes implemented under FTP 2015- 20. While some schemes such as the MEIS scheme may face discontinuation; the fate of the other schemes hang in balance. MEIS may be replaced with the much anticipated RoDTEP scheme (Remissions of Duties and Taxes on Exported Products). The RoDTEP is compatible with the requirements of WTO's Subsidies and Countervailing Measures (SCM) which prohibits a governments, especially those from a certain level of government, from providing financial services to exporters in the form of incentives. There is considerable expectation that the new policy may provide boost to export of R& D services. Another area of speculation is the EOU scheme. This scheme was also not found to be compliant with the WTO mandate. Amidst these expectations and speculations, the advent of new foreign trade policy was deferred with a government notification extending the current FTP 2015-20 till September 20, 2021

Source: <https://www.businesstoday.in/latest/economy-politics/story/govt-extends-current-foreign-trade-policy-till-sept-30-292244-2021-03-31>

Check Your Progress – 2 6. Foreign Trade policy will be henceforth reviewed every:

a. 1 year b. 2½ years c. 3 years d. 4½ years e. 10 years

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EXIM Bank provides term loans to projects located in which of the following zones? a. Trade zones b. 100% Export-oriented units in Free trade zones c. Import zones d. Export zones e. Special zones 8. Which of the following is not a guarantee issued by EXIM Bank?

a. Bid bond guarantee b. Post-payment guarantee c. Retention money guarantee d. Performance guarantee e. Guarantee for borrowing abroad 9. Which of the following is a pre-shipment finance? a. Advance against cheques b. Packing credit c. Advance against incentives receivable from government d. Advance against cheques and packing credit e. Advance against export on consignment basis 10. Which of the following is not a main objective of the foreign trade policy (2015-20)? a. To increase India's share in world exports from 4% to 5.5% by 2020. b. To provide a stable and sustained policy environment for export of merchandise and services. c. To connect varied policies, procedures, and guidelines of foreign trade with other major initiatives such as "Make in India", "Digital India" and "Skill India" to create an "Export Promotion Mission" for India. d. To widen export product basket by identifying new sectors that have potential. e. To provide a mechanism for regular appraisal for rationalizing imports and reducing trade imbalance. 14.10 Summary ? Financial management of a company is a complex process, involving its own methods and procedures. It is made even more complex because of globalization, which makes the global financial and commodity markets more and more integrated. The integration is both across countries as well as markets.

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Globalization is providing lots of opportunities to grow in the arena of international trade along with various threats which need to be overcome. ? Effective integration of financial markets demonstrates better transfer of resources between surplus units and deficit units. Capital-rich countries experience lower return on capital compared to capital-poor countries. On the other hand, integration also involves risks such as currency risk, country risk, market risk and other kinds of risks. ? The International trade of any country is divided into two types of trade: Exports: Exporting goods or services to overseas countries requires adherence to several regulatory guidelines and procedural formalities and Imports – that refers to purchase of goods or services from other countries within the framework of Export Import Policy. ? The regulatory framework for International Trade in India comprises of FEMA, Foreign Trade Policy/Exim Policy and FEDAI rules. ? FEMA Act was formulated in 1999 and replaced the erstwhile FERA (Foreign Exchange Regulation Act). The Act liberalized the exchange controls on foreign investment. Under FEMA, the emphasis is on management of foreign exchange resources. It brought clear distinction between current account and capital account transactions. ?

98%

MATCHING BLOCK 170/173

SA Summer Internship_Yamini Kalwani_249.doc (D21543163)

Foreign Exchange Dealers Association of India (FEDAI) was set up in 1958 as an association of banks dealing in foreign exchange in India (typically called Authorised Dealers –ADs) as a self-regulatory body and is incorporated under Section 25 of The Companies Act, 1956. ?

Foreign Trade Policy 2015-20 has consolidated all previous export schemes under MEIS and SEIS. The new policy is aligned to Make in India, Digital India, and Skills India initiatives. To make India's export of goods and services globally competitive and double exports by 2020, a plethora of schemes have been introduced. ? Exim Policy will be announced by DGFT Ministry of Commerce Exports and imports are allowed within the framework of Trade Policy, Exchange Control Norms and FEMA. IEC code number will be provided by DGFT ? Banks play a significant role in providing import finance according to exchange control guidelines. Pre-shipment finance and post-shipment finance will be provided by banks to the eligible exporters ? An importer's request to open a letter of credit is carefully examined by a bank in terms of trade control requirements, exchange control requirements, credit norms of RBI, UCPDC provisions, FEDAI guidelines, and lastly internal procedures of bank.

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Glossary Authorized Dealers are persons designated as an authorized dealer under sub- section (1) of section 10 of the FEMA Act. It also refers to a person designated as an authorized dealer under sub-section (1) of section 10 of the FEMA Act and includes a person carrying on business as a factor. Bill of Lading is a legal document that is drawn between the shipper of goods and the carrier specifying the type, quantity and destination of goods on board the ship/carrier. It is a negotiable instrument. Country Risk is the risk perceived by a non-resident while dealing with a country in a commercial and/or investment transaction, which arises out of political and economic factors. Currency Swap is a contract involving exchange of interest payments on a loan in one currency for fixed or floating interest payments on equivalent loan in a different currency. Deemed Exports are those that occur in case of specified transactions within India, which result in foreign exchange earnings or savings. Duty Drawback means the rebate of duty chargeable on imported material or excisable material used in the manufacturing of goods that is to be exported. The exporter may claim drawback or refund of excise and customs duties being paid by his suppliers. Export Oriented Units (EOU) units that are set up for export promotion. An EOU can be set up by any entrepreneur for manufacturing of goods and also for rendering services. An EOU can be set up for repair, reconditioning, re-making and re-engineering also.

76%**MATCHING BLOCK 173/173****SA**

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FEDAI set up in 1958 is an association of banks dealing in foreign exchange in India (typically called Authorised Dealers —ADs). It is a self-regulatory body and its major activities include framing of rules governing the conduct of inter- bank foreign exchange business among banks vis-à-vis public and liaison with RBI for reforms and development of forex market.

Forfeiting is a common form of financing export-related receivables.

It is similar to Bill Rediscounting Scheme. EXIM Bank has introduced this scheme for the Indian exporters. Future Contracts is a contract which is exchange traded subjected to losses/gains arriving out of daily changes in underlying asset such as foreign currencies or commodities. Globalization is the opening up of local and domestic perspectives to a broader outlook of an inter-connected and inter-dependent world that encourages free transfer of goods, services and capital beyond national boundaries.

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Import Export Code (IEC) is a ten digit importer exporter code number (IEC Number) allotted by DGFT. Interest Rate Swap means an agreement between two or more parties to exchange interest payments over a specific time period on agreed terms. International Finance is the study of exchange rates, foreign investment and their effect on

96%**MATCHING BLOCK 171/173****W**

international trade. International Trade is the exchange of goods and services across international boundaries.

Option is a contract in which the seller grants the buyer, the right to purchase from the seller a designated instrument or an asset at a specific price which is agreed upon at the time of entering into the contract. Pre-shipment Finance is any advance or loan or any credit extended to exporters by a bank either in domestic or foreign currency for the purpose of manufacturing, procuring, processing or packing of goods before shipment. Post-shipment Finance is provided to finance export sale receivables of the exporter. It can be defined

71%**MATCHING BLOCK 172/173****W**

as any loan or advance granted or any other credit provided by an institution to an exporter from India.

Directorate General of Foreign Trade (DGFT) is a government organization entrusted with the responsibility of framing all policies related to exports and imports. Domestic Tariff Area means area within India which is outside SEZs and EOU/EHTP/STP/BTP. Export Obligation means obligation to export product or products covered by authorization or permission in terms of quantity, value or both, as may be prescribed or specified by a regional or competent authority. Special Economic Zone (SEZ) is a geographical region that has economic laws different from a country's typical economic laws. Usually, the goal is to increase foreign investments. Status Holder means an exporter recognized as

One Star Export House/Two Star Export House/Three Star Export House/Four Star Export House/Five Star Export House

by DGFT/Development Commissioner. UCPDC or Uniform Customs and Practice for Documentary Credits are guidelines issued by the International Chamber of Commerce (ICC) to provide uniform interpretation of terminology used under documentary credit. The latest version of the rules that govern L/C transactions worldwide is UCP600 effective since 1 July 2007.

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Self-Assessment Test 1. Explain the significance of studying international finance. 2. What is integration of markets? Discuss the reasons, benefits and costs associated with integration. 3. Broadly explain the three major themes of current Foreign Trade Policy. 4. Explain the general provisions relating to imports/exports in the new Foreign Trade Policy. 5. Explain pre-shipment finance and post-shipment finance provided to the exporters. 6. Discuss in detail the pre-requisites for opening an import Letter of Credit. 7. How does customs clearance of imports into India take place? 14.13

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Answers to Check Your Progress Questions 1. (e) All companies need to understand international finance Companies having international operations are not the only ones which need to be aware of the complexities of international finance. Even companies operating domestically need to understand the issues involved. 2. (e) Both domestic currency and internationally accepted currency The settlement currency may either be the domestic currency of one of the parties to the trade, or may be an internationally accepted currency. 3. (b) Securities are not correlated Diversification is possible when securities are not correlated. 4. (c) Globalization Integration of financial markets across geographical boundaries is called globalization. 5. (e) Debentures Globalization led to the development of currency swaps, interest rate swaps, futures, and options. 6. (b) 2½ years Foreign Trade Policy will be reviewed after 2½ years moving away from the tradition of annual reviews. 7. (b) 100% export oriented units in Free Trade Zones EXIM Bank provides term loans to projects located in free trade zones. 8. (b) Post-payment guarantee The guarantees provided by EXIM Bank are bid bond guarantee, advance payment guarantee, performance guarantee, retention money guarantee, and guarantee for borrowing abroad. 9. (d) Advance against cheques and packing credit Pre-shipment finance consists of advance against cheques and packing credit.

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a) To increase India's share in world exports from 4% to 5.5% by 2020 The objectives of Foreign Trade Policy (2015-20) are: ? To increase India's share in world exports from 2% to 3.5% by 2020. ? To provide a stable and sustained policy environment for export of merchandise and services. ? To connect varied policies, procedures, and guidelines of foreign trade with other major initiatives such as "Make in India", "Digital India", and "Skill India" to create an "Export Promotion Mission" for India. ? To widen export product basket by identifying new sectors that have potential. ? To provide a mechanism for regular appraisal for rationalizing imports and reducing trade imbalance.

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Appendix 1:

Interest Rate Tables Table1: Future Value Interest Factor n/k 1% 2% 3% 4% 5% 6% 7% 8% 9% 10% 11% 12% 13% 0 1.000 1.000 1.000
1.000 1.000 1.000 1.000 1.000 1.000 1.000 1.000 1.000 1.000 1.000 1 1.010 1.020 1.030 1.040 1.050 1.060 1.070 1.080 1.090 1.100 1.110
1.120 1.130 2 1.020 1.040 1.061 1.082 1.102 1.124 1.145 1.166 1.188 1.210 1.232 1.254 1.277 3 1.030 1.061 1.093 1.125 1.158 1.191 1.225
1.260 1.295 1.331 1.368 1.405 1.443 4 1.041 1.082 1.126 1.170 1.216 1.262 1.311 1.360 1.412 1.464 1.518 1.574 1.630 5 1.051 1.104 1.159
1.217 1.276 1.338 1.403 1.469 1.539 1.611 1.685 1.762 1.842 6 1.062 1.126 1.194 1.265 1.340 1.419 1.501 1.587 1.677 1.772 1.870 1.974
2.082 7 1.072 1.149 1.230 1.316 1.407 1.504 1.606 1.714 1.828 1.949 2.076 2.211 2.353 8 1.083 1.172 1.267 1.369 1.477 1.594 1.718 1.851
1.993 2.144 2.305 2.476 2.658 9 1.094 1.195 1.305 1.423 1.551 1.689 1.838 1.999 2.172 2.358 2.558 2.773 3.004 10 1.105 1.219 1.344
1.480 1.629 1.791 1.967 2.159 2.367 2.594 2.839 3.106 3.395 11 1.116 1.243 1.384 1.539 1.710 1.898 2.105 2.332 2.580 2.853 3.152
3.479 3.836 12 1.127 1.268 1.426 1.601 1.796 2.012 2.252 2.518 2.813 3.138 3.498 3.896 4.335 13 1.138 1.294 1.469 1.665 1.886 2.133
2.410 2.720 3.066 3.452 3.883 4.363 4.898 14 1.149 1.319 1.513 1.732 1.980 2.261 2.579 2.937 3.342 3.797 4.310 4.887 5.535 15 1.161
1.346 1.558 1.801 2.097 2.397 2.759 3.172 3.642 4.177 4.785 5.474 6.254 16 1.173 1.373 1.605 1.873 2.183 2.540 2.952 3.426 3.970
4.595 5.311 6.130 7.067 17 1.184 1.400 1.653 1.948 2.292 2.693 3.159 3.700 4.328 5.054 5.895 6.866 7.986 18 1.196 1.428 1.702 2.026
2.407 2.854 3.380 3.996 4.717 5.560 6.544 7.690 9.024 19 1.208 1.457 1.754 2.107 2.527 3.026 3.617 4.316 5.142 6.116 7.263 8.613
10.197 20 1.220 1.486 1.806 2.191 2.653 3.207 3.870 4.661 5.604 6.728 8.062 9.646 11.523 25 1.282 1.641 2.094 2.666 3.386 4.292
5.427 6.848 8.623 10.835 13.585 17.000 21.231 30 1.348 1.811 2.427 3.243 4.322 5.743 7.612 10.063 13.268 17.449 22.892 29.960
39.116

214 Table 1: Future Value Interest Factor n/k 14% 15% 16% 17% 18% 19% 20% 24% 28% 32% 36% 40% 0 1.000 1.000 1.000 1.000 1.000
1.000 1.000 1.000 1.000 1.000 1.000 1.000 1 1.140 1.150 1.160 1.170 1.180 1.190 1.200 1.240 1.280 1.320 1.360 1.400 2 1.300 1.322
1.346 1.369 1.392 1.416 1.440 1.538 1.638 1.742 1.850 1.960 3 1.482 1.521 1.561 1.602 1.643 1.685 1.728 1.907 2.097 2.300 2.515 2.744
4 1.689 1.749 1.811 1.874 1.939 2.005 2.074 2.364 2.684 3.036 3.421 3.842 5 1.925 2.011 2.100 2.192 2.288 2.386 2.488 2.392 3.436
4.007 4.653 5.378 6 2.195 2.313 2.436 2.565 2.700 2.840 2.986 3.635 4.398 5.290 6.328 7.530 7 2.502 2.660 2.826 3.001 3.185 3.379
3.583 4.508 5.629 6.983 8.605 10.541 8 2.853 3.059 3.278 3.511 3.759 4.021 4.300 5.590 7.206 9.217 11.703 14.758 9 3.252 3.518
3.803 4.108 4.435 4.785 5.160 6.931 9.223 12.166 15.917 20.661 10 3.707 4.046 4.411 4.807 5.234 5.695 6.192 8.594 11.806 16.060
21.647 28.925 11 4.226 4.652 5.117 5.624 6.176 6.777 7.430 10.657 15.112 21.199 29.439 40.496 12 4.818 5.350 5.936 6.580 7.288
8.064 8.916 13.215 19.343 27.983 40.037 56.694 13 5.492 6.153 6.886 7.699 8.599 9.596 10.699 16.386 24.759 36.937 54.451 79.372
14 6.261 7.076 7.988 9.007 10.147 11.420 12.839 20.319 31.961 48.757 74.053 111.120 15 7.138 8.137 9.266 10.539 11.974 13.590 15.407
25.196 40.565 64.359 100.712 155.568 16 8.137 9.358 10.748 12.330 14.129 16.172 18.488 31.243 51.923 84.954 136.969 217.795 17
9.276 10.761 12.468 14.426 16.672 19.244 22.186 38.741 66.461 112.139 186.278 304.914 18 10.575 12.375 14.463 16.879 19.673 22.901
26.623 48.039 85.071 148.023 253.338 426.879 19 12.056 14.232 16.777 19.748 23.214 27.252 31.948 59.568 108.890 195.391
344.540 597.630 20 13.743 16.367 19.461 23.106 27.393 32.429 38.338 73.864 139.380 257.916 468.574 836.683 25 26.462 32.919
40.874 50.658 62.669 77.388 95.396 216.542 478.905 1033.590 2180.081 4499.880 30 50.950 66.212 85.850 111.065 143.371
184.675 237.376 634.820 1645.504 4142.075 10143.019 24201.432

215 Table 2: Future

Value Interest Factor for an Annuity n/k	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	11%	12%	13%	1	1.000	1.000	1.000	1.000	1.000	1.000	1.000	
1.000	1.000	1.000	1.000	1.000	1.000	2	2.010	2.020	2.030	2.040	2.050	2.060	2.070	2.080	2.090	2.100	2.110	2.120	2.130	3	3.030	
3.060	3.091	3.122	3.152	3.184	3.215	3.246	3.278	3.310	3.342	3.374	3.407	4	4.060	4.122	4.184	4.246	4.310	4.375	4.440	4.506	4.573	
4.641	4.710	4.779	4.850	5	5.101	5.204	5.309	5.416	5.526	5.637	5.751	5.867	5.985	6.105	6.228	6.353	6.480	6	6.152	6.308	6.468	6.633
6.802	6.975	7.153	7.336	7.523	7.716	7.913	8.115	8.323	7	7.214	7.434	7.662	7.898	8.142	8.394	8.654	8.923	9.200	9.487	9.783	10.089	
10.405	8	8.286	8.583	8.892	9.214	9.549	9.897	10.260	10.637	11.028	11.436	11.859	12.300	12.757	9	9.369	9.755	10.159	10.583	11.027		
11.491	11.978	12.488	13.021	13.579	14.164	14.776	15.416	10	10.462	10.950	11.464	12.006	12.578	13.181	13.816	14.487	15.193	15.937				
16.722	17.549	18.420	11	11.567	12.169	12.808	13.486	14.207	14.972	15.784	16.645	17.560	18.531	19.561	20.655	21.814	12	12.683	13.412			
14.192	15.026	15.917	16.870	17.888	18.977	21.141	21.384	22.713	24.133	25.650	13	13.809	14.680	15.618	16.627	17.713	18.882	20.141				
21.495	22.953	24.523	26.212	28.029	29.985	14	14.947	15.974	17.086	18.292	19.599	21.015	22.550	24.215	26.019	27.975	30.095	32.393				
34.883	15	16.097	17.293	18.599	20.024	21.579	23.276	25.129	27.152	29.361	31.772	34.405	37.280	40.417	16	17.258	18.639	20.157				
21.825	23.657	25.673	27.888	30.324	33.003	35.950	39.190	42.753	46.672	17	18.430	20.012	21.762	23.698	25.840	28.213	30.840					
33.750	36.974	40.545	44.501	48.884	53.739	18	19.615	21.412	23.414	25.645	28.132	30.906	33.999	37.450	41.301	45.599	50.396					
55.750	61.725	19	20.811	22.841	25.117	27.671	30.539	33.760	37.379	41.446	46.018	51.159	56.939	63.440	70.749	20	22.019	24.297				
26.870	29.778	33.066	36.786	40.995	45.762	51.160	57.275	64.203	72.052	80.947	25	28.243	32.030	36.459	41.646	47.727	54.865					
63.249	73.106	84.701	98.347	114.413	133.334	155.620	30	34.785	40.568	47.575	56.805	66.439	79.058	94.461	113.283	136.308						
164.494	199.021	241.333	293.199																			

216 Table 2: Future Value Interest Factor for an Annuity n/k																							14%	15%	16%	17%	18%	19%	20%	24%	28%	32%	36%	40%	1	1.000	1.000
1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	2	2.140	2.150	2.160	2.170	2.180	2.190	2.200	2.240	2.280	2.320	2.360																
2.400	3	3.440	3.473	3.506	3.539	3.572	3.606	3.640	3.778	3.918	4.062	4.210	4.360	4	4.921	4.993	5.066	5.141	5.215	5.291	5.368	5.684															
6.016	6.362	6.725	7.104	5	6.610	6.742	6.877	7.014	7.154	7.297	7.442	8.048	8.700	9.398	10.146	10.946	6	8.536	8.754	8.977	9.207	9.442															
9.683	9.930	10.980	12.136	13.406	14.799	16.324	7	10.730	11.067	11.414	11.772	12.142	12.523	12.916	14.615	16.534	18.696	21.126																			
23.853	8	13.233	13.727	14.240	14.773	15.327	15.902	16.499	19.123	22.163	25.678	29.732	34.395	9	16.085	16.786	17.518	18.285	19.086																		
19.923	20.799	24.712	29.369	34.895	41.435	49.153	10	19.337	20.304	21.321	22.393	23.521	24.709	25.959	31.643	38.592	47.062	57.352																			
69.814	11	23.044	24.349	25.733	27.200	28.755	30.404	32.150	40.238	50.399	63.122	78.998	98.739	12	27.271	29.002	30.850	32.824																			
34.931	37.180	39.580	50.985	65.510	84.320	108.437	139.235	13	32.089	34.352	36.786	39.404	42.219	45.244	48.497	64.110	84.853																				
112.303	148.475	195.929	14	37.581	40.505	43.672	47.103	50.818	54.841	59.196	80.496	109.612	149.240	202.926	275.300	15	43.842																				
47.580	51.660	56.110	60.965	66.261	72.035	100.815	141.303	197.997	276.979	386.420	16	50.980	55.717	60.925	66.649	72.939	79.850																				
87.442	126.011	181.868	262.356	377.692	541.988	17	59.118	65.075	71.673	78.979	87.068	96.022	105.931	157.253	233.791	347.310																					
514.661	759.784	18	68.394	75.836	84.141	93.406	103.740	115.266	128.117	195.994	300.252	459.449	700.939	1064.697	19	78.969																					
88.212	98.603	110.285	123.414	138.166	154.740	244.033	385.323	607.472	954.277	1491.576	20	91.025	102.44	115.380	130.033																						
146.628	165.418	186.688	303.601	494.213	802.863	1298.817	2089.206	25	181.871	212.793	249.214	292.105	342.603	402.042	371.981																						
898.092	1706.803	3226.844	6053.004	11247.199	30	356.787	434.745	530.321	647.439	790.948	966.712	1181.882	2640.916	5873.231																							
12940.859	28172.276	60501.081																																			

217 Table 3: Present Value Interest Factor

n/k	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	11%	12%	13%	0	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000				
1.000	1	0.990	0.980	0.971	0.962	0.952	0.943	0.935	0.926	0.917	0.909	0.901	0.893	0.885	2	0.980	0.961	0.943	0.925	0.907	0.890										
0.873	0.857	0.842	0.826	0.812	0.797	0.783	3	0.971	0.942	0.915	0.889	0.864	0.840	0.816	0.794	0.772	0.751	0.731	0.712	0.693	4	0.961									
0.924	0.889	0.855	0.823	0.792	0.763	0.735	0.708	0.683	0.659	0.636	0.613	5	0.951	0.906	0.863	0.822	0.784	0.747	0.713	0.681	0.650										
0.621	0.593	0.567	0.543	6	0.942	0.888	0.838	0.790	0.746	0.705	0.666	0.630	0.596	0.564	0.535	0.507	0.480	7	0.933	0.871	0.813										
0.760	0.711	0.665	0.623	0.583	0.547	0.513	0.482	0.452	0.425	8	0.923	0.853	0.789	0.731	0.677	0.627	0.582	0.540	0.502	0.467	0.434										
0.404	0.376	9	0.914	0.873	0.766	0.703	0.645	0.592	0.544	0.500	0.460	0.424	0.391	0.361	0.333	10	0.905	0.820	0.744	0.676	0.614										
0.558	0.508	0.463	0.422	0.386	0.352	0.322	0.295	11	0.896	0.804	0.722	0.650	0.585	0.527	0.475	0.429	0.388	0.350	0.317	0.287	0.261										
12	0.887	0.788	0.701	0.625	0.557	0.497	0.444	0.397	0.356	0.319	0.286	0.257	0.231	13	0.879	0.773	0.681	0.601	0.530	0.469	0.415										
0.368	0.326	0.290	0.258	0.229	0.204	14	0.870	0.758	0.661	0.577	0.505	0.442	0.388	0.340	0.299	0.263	0.232	0.181	0.205	15	0.861										
0.743	0.642	0.555	0.481	0.417	0.362	0.315	0.275	0.239	0.209	0.183	0.160	16	0.853	0.728	0.623	0.534	0.458	0.394	0.339	0.292	0.252										
0.218	0.188	0.163	0.141	17	0.844	0.714	0.605	0.513	0.436	0.371	0.317	0.270	0.231	0.198	0.170	0.146	0.125	18	0.836	0.700	0.587	0.494									
0.416	0.350	0.296	0.250	0.212	0.180	0.153	0.130	0.111	19	0.828	0.686	0.570	0.475	0.396	0.331	0.276	0.232	0.194	0.164	0.138	0.166										
0.098	20	0.820	0.673	0.554	0.456	0.377	0.312	0.258	0.215	0.178	0.149	0.124	0.104	0.087	25	0.780	0.610	0.478	0.375	0.295	0.233										
0.184	0.146	0.116	0.092	0.074	0.059	0.047	30	0.742	0.552	0.412	0.308	0.231	0.174	0.131	0.099	0.075	0.057	0.044	0.033	0.026											
218	Table 3: Present Value Interest Factor n/k														14%	15%	16%	17%	18%	19%	20%	24%	28%	32%	36%	40%	0	1.000	1.000	1.000	1.000
1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1	0.877	0.870	0.862	0.855	0.847	0.840	0.833	0.806	0.781	0.758	0.735	0.714	2	0.769									
0.756	0.743	0.731	0.718	0.706	0.694	0.650	0.610	0.574	0.541	0.510	3	0.675	0.658	0.641	0.624	0.609	0.593	0.579	0.524	0.477	0.435										
0.398	0.364	4	0.592	0.572	0.552	0.534	0.516	0.499	0.482	0.423	0.373	0.329	0.292	0.260	5	0.519	0.497	0.476	0.456	0.437	0.419	0.402									
0.341	0.291	0.250	0.215	0.186	6	0.456	0.432	0.410	0.390	0.370	0.352	0.335	0.275	0.227	0.189	0.158	0.133	7	0.400	0.376	0.354	0.333									
0.314	0.296	0.279	0.222	0.178	0.143	0.116	0.095	8	0.351	0.327	0.305	0.285	0.266	0.249	0.233	0.179	0.139	0.108	0.085	0.068	9	0.308									
0.284	0.263	0.243	0.226	0.209	0.194	0.144	0.108	0.082	0.063	0.048	10	0.270	0.247	0.227	0.208	0.191	0.176	0.162	0.116	0.085	0.062										
0.046	0.035	11	0.237	0.215	0.195	0.178	0.162	0.148	0.135	0.094	0.066	0.047	0.034	0.025	12	0.208	0.187	0.168	0.152	0.137	0.124	0.112									
0.076	0.052	0.036	0.025	0.018	13	0.182	0.163	0.145	0.130	0.116	0.104	0.093	0.061	0.040	0.027	0.018	0.013	14	0.160	0.141	0.125	0.111									
0.099	0.088	0.078	0.049	0.032	0.021	0.014	0.009	15	0.140	0.123	0.108	0.095	0.084	0.074	0.065	0.040	0.025	0.016	0.010	0.006	16										
0.123	0.107	0.093	0.081	0.071	0.062	0.054	0.032	0.019	0.012	0.005	0.007	17	0.108	0.093	0.080	0.069	0.060	0.052	0.045	0.026	0.015										
0.009	0.005	0.003	18	0.095	0.081	0.069	0.059	0.051	0.044	0.038	0.021	0.012	0.007	0.004	0.002	19	0.083	0.070	0.060	0.051	0.043										
0.037	0.031	0.017	0.009	0.005	0.003	0.002	20	0.073	0.061	0.051	0.043	0.037	0.031	0.026	0.014	0.007	0.004	0.002	0.001	25	0.038										
0.030	0.024	0.020	0.016	0.013	0.010	0.005	0.002	0.001	0.000	0.000	30	0.020	0.015	0.012	0.009	0.007	0.005	0.004	0.002	0.001											
0.000	0.000	0.000																													

[illegible]

//secure.urkund.com/view/158576956-568953-794338#/sources 184/230

Financial Management Process 11. Financial System – Indian and International Scenario 12. Time Value of Money 13. Sources of Short Term and Long Term Finance 14. Basics of International Trade and Finance

Hit and source - focused comparison, Side by Side

Submitted text		As student entered the text in the submitted document.	
Matching text		As the text appears in the source.	
1/173	SUBMITTED TEXT	45 WORDS	84% MATCHING TEXT 45 WORDS
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3/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
	Central Public Sector Enterprises ETF runs a concentrated portfolio with		Central Public Sector Enterprises ETF runs a concentrated portfolio with	
	W https://www.livemint.com/market/stock-market-news/govt-plans-to-garner-rs-10-000-cr-from-7th-tran ...			
4/173	SUBMITTED TEXT	14 WORDS	88% MATCHING TEXT	14 WORDS
	energy and oil sector. Nippon Life India Asset Management company (formerly known as		energy and oil sector. Nippon Life India Asset Management, formerly known as	
	W https://www.livemint.com/market/stock-market-news/govt-plans-to-garner-rs-10-000-cr-from-7th-tran ...			
5/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
	Reliance Nippon Life Asset Management) is managing the CPSE-ETF on		Reliance Nippon Life Asset Management, is managing the CPSE ETF on	
	W https://www.livemint.com/market/stock-market-news/govt-plans-to-garner-rs-10-000-cr-from-7th-tran ...			
6/173	SUBMITTED TEXT	18 WORDS	100% MATCHING TEXT	18 WORDS
	ONGC, NTPC, Coal India, IOC, REC, PFC, Bharat Electronics, Oil India, NBCC India, NLC India and SJVN.		ONGC, NTPC, Coal India, IOC, REC, PFC, Bharat Electronics, Oil India, NBCC India, NLC India and SJVN.	
	W https://www.livemint.com/market/stock-market-news/govt-plans-to-garner-rs-10-000-cr-from-7th-tran ...			

7/173	SUBMITTED TEXT	25 WORDS	64% MATCHING TEXT	25 WORDS
	The proceeds from this offer will enable the Government to meet its disinvestment target of ₹ 1.05 lakh crore 2 .		The proceeds from the ETF will help the government meet its disinvestment target of ₹1.05 lakh crore	
	W https://www.livemint.com/market/stock-market-news/govt-plans-to-garner-rs-10-000-cr-from-7th-tran ...			
8/173	SUBMITTED TEXT	1 WORDS	87% MATCHING TEXT	1 WORDS
	govt-plans-to-garner-rs-10-000- cr-from-7th-tranche-of-cpse-etf-11579784581897.		Govt plans to garner ₹10,000 cr from 7th tranche of CPSE ETF	
	W https://www.livemint.com/market/stock-market-news/govt-plans-to-garner-rs-10-000-cr-from-7th-tran ...			
9/173	SUBMITTED TEXT	1 WORDS	100% MATCHING TEXT	1 WORDS
	markets/stocks/earnings/nestle-q1-results-net- profit-rises-15-yoy-to-rs-602-crore-beats-estimates/		Markets>Stocks>Earnings>Nestle Q1 results: Net profit rises 15% YoY to Rs 602 crore, beats estimates	
	W https://economictimes.indiatimes.com/markets/stocks/earnings/nestle-q1-results-net-profit-rises-1 ...			

10/173	SUBMITTED TEXT	181 WORDS	92% MATCHING TEXT	181 WORDS
	<p>Bajaj Finance surpasses SBI in Market Capitalization On 24th August 2021, the shares of Bajaj Finance traded 3.40 % higher at ₹ 6,983.35 a share on BSE, taking its market cap to ₹ 4.22 lakh crore, surpassing that of SBI's ₹ 3.71 lakh crore as the latter's shares traded up only by 1.56% at ₹ 415.70 a share. This is not the first time that this non-banking finance firm overtook India's biggest lender by assets. Bajaj Finance, on 1 st October 2019, was trading on BSE at ₹3,992.20, taking its market cap to ₹2.32 lakh crore. On that day the price of SBI, fell to ₹254.55 a share, bringing down its market cap to ₹2.28 lakh crore, falling behind Bajaj Finance. At that time Bajaj had a total loan book of ₹1.25 lakh crore, while SBI's stood at ₹22.40 lakh crore. On 17 th Feb 2020, and again on 22 nd June 2020 Bajaj Finance pipped SBI in market capitalisation.</p>		<p>Bajaj Finance Surpasses SBI in Market Cap September 2, 2021September 2, 2021 Icfai BytesIcfai Bytes 0 Comments On 24th August 2021, the shares of Bajaj Finance [1] traded 3.40 % higher at ₹ 6,983.35 a share on BSE, taking its market cap to ₹ 4.22 lakh crore, surpassing that of SBI's ₹ 3.71 lakh crore as the latter's shares traded up only by 1.56% at ₹ 415.70 a share. Is This the First Time? This is not the first time that this non-banking finance firm [2]overtook India's biggest lender by assets. Bajaj Finance, on 1st October 2019, was trading on BSE at ₹3,992.20, taking its market cap to ₹2.32 lakh crore. On that day the price of SBI, fell to ₹254.55 a share, bringing down its market cap to ₹2.28 lakh crore, falling behind Bajaj. At that time Bajaj had a total loan book of ₹1.25 lakh crore, while SBI's stood at ₹22.40 lakh crore. On 17th Feb 2020 [3], and again on 22nd June 2020 [4]Bajaj pipped SBI in market capitalisation.</p>	
	<p>W https://icfaibytes.in/2021/09/02/bajaj-finance-surpasses-sbi-in-market-cap/</p>			
11/173	SUBMITTED TEXT	29 WORDS	100% MATCHING TEXT	29 WORDS
	<p>has cracked the code in consumer lending. Despite most of its loans being unsecured, for its mastery in the art of pricing risk, asset quality metrics of Bajaj</p>		<p>has cracked the code in consumer lending. Despite most of its loans being unsecured, for its mastery in the art of pricing risk, asset quality metrics of Bajaj</p>	
	<p>W https://icfaibytes.in/2021/09/02/bajaj-finance-surpasses-sbi-in-market-cap/</p>			
12/173	SUBMITTED TEXT	18 WORDS	100% MATCHING TEXT	18 WORDS
	<p>The consistent and far better earnings of Bajaj have made the share highly palatable to investors.</p>		<p>The consistent and far better earnings of Bajaj have made the share highly palatable to investors.</p>	
	<p>W https://icfaibytes.in/2021/09/02/bajaj-finance-surpasses-sbi-in-market-cap/</p>			

13/173	SUBMITTED TEXT	45 WORDS	76% MATCHING TEXT	45 WORDS
<p>All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, used in a spreadsheet, or transmitted in any form or by any means – electronic, mechanical, photocopying or otherwise – without prior permission in writing from The</p> <p>SA BANK SYSTEM.pdf (D133233577)</p>				
14/173	SUBMITTED TEXT	16 WORDS	96% MATCHING TEXT	16 WORDS
<p>PFM) is an essential aspect of the institutional framework for an effective state. 7</p> <p>W http://www.gsdr.org/professional-dev/public-financial-management/</p>				
15/173	SUBMITTED TEXT	96 WORDS	95% MATCHING TEXT	96 WORDS
<p>PFM refers to the set of laws, rules, systems and processes used by sovereign nations (and sub-national governments), to mobilize revenue, allocate public funds, undertake public spending, account for funds and audit results. It 7</p> <p>W http://www.gsdr.org/professional-dev/public-financial-management/</p>				
16/173	SUBMITTED TEXT	20 WORDS	100% MATCHING TEXT	20 WORDS
<p>encompasses a broader set of functions than financial management and is commonly conceived as a cycle of six phases-</p> <p>W http://www.gsdr.org/professional-dev/public-financial-management/</p>				

17/173	SUBMITTED TEXT	13 WORDS	87% MATCHING TEXT	13 WORDS
<p>by measuring the standard deviation of the historical returns or average returns</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				
18/173	SUBMITTED TEXT	18 WORDS	100% MATCHING TEXT	18 WORDS
<p>Securities A Government security is a tradable instrument issued by the Central Government or the State Governments.</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				
19/173	SUBMITTED TEXT	40 WORDS	80% MATCHING TEXT	40 WORDS
<p>original maturities of less than one year. The long-term Government bonds or dated securities have original maturity of one year or more. In India, the Central Government issues both treasury bills and bonds or dated securities State Governments</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				
20/173	SUBMITTED TEXT	16 WORDS	90% MATCHING TEXT	16 WORDS
<p>carry a fixed or floating coupon (interest rate) paid on the face value and is</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				

21/173	SUBMITTED TEXT	17 WORDS	100% MATCHING TEXT	17 WORDS
<p>securities are issued through auctions conducted by the RBI on the electronic platform called the NDS.</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				
22/173	SUBMITTED TEXT	34 WORDS	85% MATCHING TEXT	34 WORDS
<p>of India acts as the registry / depository of Government securities and deals with the issue, interest payment and repayment of principal on maturity. Most of the dated securities are fixed coupon securities.</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				
23/173	SUBMITTED TEXT	13 WORDS	83% MATCHING TEXT	13 WORDS
<p>no interest. However, they are issued at a discount and redeemed at</p> <p>SA book fm(1).doc (D144076294)</p>				
24/173	SUBMITTED TEXT	18 WORDS	73% MATCHING TEXT	18 WORDS
<p>pay no interest. However, they are issued at a discount and redeemed at the face value at</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				

25/173	SUBMITTED TEXT	21 WORDS	54% MATCHING TEXT	21 WORDS
<p>day and 364 day tenure T-bills are auctioned on alternate Wednesdays. The Reserve Bank releases an annual calendar of T-bill</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>				
26/173	SUBMITTED TEXT	12 WORDS	100% MATCHING TEXT	12 WORDS
<p>Government of India, in consultation with the Reserve Bank of India,</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				
27/173	SUBMITTED TEXT	13 WORDS	87% MATCHING TEXT	13 WORDS
<p>to meet the temporary mismatches in the cash flow of the Government.</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				
28/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
<p>in consumer goods, real estate, agriculture, chemicals and financial services</p> <p>W https://www.godrejindustries.com/know-us/our-story#footer</p>				

29/173	SUBMITTED TEXT	17 WORDS	87% MATCHING TEXT	17 WORDS
Commercial papers (CP) -an unsecured money market instrument issued in the form of a promissory note.		Commercial Papers (CPs): Commercial Paper (CP) an unsecured money market instrument issued in the form of a promissory note		
W http://dimr.edu.in/wp-content/uploads/2020/05/205-Fin-notes.pdf				
30/173	SUBMITTED TEXT	30 WORDS	100% MATCHING TEXT	30 WORDS
Government of India also issues savings instruments (Savings Bonds, National Saving Certificates (NSCs), etc.) or special securities (oil bonds, Food Corporation of India bonds, fertilizer bonds, power bonds, etc.).				
SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)				
31/173	SUBMITTED TEXT	18 WORDS	85% MATCHING TEXT	18 WORDS
Commercial papers (CP) -an unsecured money market instrument issued in the form of a promissory note. It				
SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)				
32/173	SUBMITTED TEXT	22 WORDS	88% MATCHING TEXT	22 WORDS
introduced in India in 1990 with a view to enable highly rated corporate borrowers to diversify their sources of short-term borrowings.		introduced in India January 1990. CPs were in India with a view to enable highly rated corporate borrowers to diversify their sources of short-term borrowings		
W http://dimr.edu.in/wp-content/uploads/2020/05/205-Fin-notes.pdf				

38/173	SUBMITTED TEXT	20 WORDS	77% MATCHING TEXT	20 WORDS
<p>objectives of FEMA are: (i) to facilitate external trade and payments, and (ii) to promote an orderly maintenance of</p> <p>SA Summer Internship_Yamini Kalwani_249.doc (D21543163)</p>				
39/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
<p>within a period of six months from the date of</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				
40/173	SUBMITTED TEXT	64 WORDS	84% MATCHING TEXT	64 WORDS
<div> <div> Public Finance Management PFM refers to the set of laws, rules, systems and processes used by sovereign nations (and sub-national governments), to mobilize revenue, allocate public funds, undertake public spending, account for funds and audit results. It encompasses a broader set of functions than Unit 10: Financial Management Process 59 financial management and is commonly conceived as a cycle of six phases- </div> <div> Public Financial Management (PFM)? PFM refers to the set of laws, rules, systems and processes used by sovereign nations (and sub-national governments), to mobilise revenue, allocate public funds, undertake public spending, account for funds and audit results. It encompasses a broader set of functions than financial management and is commonly conceived as a cycle of six phases, </div> </div> <p>W http://www.gsdr.org/professional-dev/public-financial-management/</p>				
41/173	SUBMITTED TEXT	24 WORDS	87% MATCHING TEXT	24 WORDS
<p>discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>				

42/173	SUBMITTED TEXT	14 WORDS	100% MATCHING TEXT	14 WORDS
<p>is a tradable instrument issued by the Central Government or the State Governments.</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				
43/173	SUBMITTED TEXT	22 WORDS	92% MATCHING TEXT	22 WORDS
<p>A financial system functions as an intermediary and facilitates the flow of funds from the areas of surplus to the</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>				
44/173	SUBMITTED TEXT	22 WORDS	92% MATCHING TEXT	22 WORDS
<p>A financial system functions as an intermediary and facilitates the flow of funds from the areas of surplus to the</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				
45/173	SUBMITTED TEXT	16 WORDS	86% MATCHING TEXT	16 WORDS
<p>A financial system is a composition of various institutions, markets, regulations and laws, practices, money</p> <p>SA book fm(1).doc (D144076294)</p>				

46/173	SUBMITTED TEXT	26 WORDS	92% MATCHING TEXT	26 WORDS
<p>areas of deficit. A financial system is a composition of various institutions, markets, regulations and laws, practices, money managers, analysts, transactions and claims and liabilities.</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>				
47/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
<p>The financial markets provide the investor with the opportunity to</p> <p>SA book fm(1).doc (D144076294)</p>				
48/173	SUBMITTED TEXT	31 WORDS	85% MATCHING TEXT	31 WORDS
<p>Payment Function The financial system offers a very convenient mode of payment for goods and services. The cheque system, credit card system et al. are the easiest methods of payments.</p> <p>SA book fm(1).doc (D144076294)</p>				
49/173	SUBMITTED TEXT	37 WORDS	59% MATCHING TEXT	37 WORDS
<p>financial system offers a very convenient mode of payment for goods and services. The cheque system, credit card system et al. are the easiest methods of payments. The cost and time of transactions are drastically reduced.</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				

50/173	SUBMITTED TEXT	12 WORDS	100%	MATCHING TEXT	12 WORDS
<p>In India, the cheque system of payment is widely practiced. The</p> <p>SA book fm(1).doc (D144076294)</p>					
51/173	SUBMITTED TEXT	14 WORDS	88%	MATCHING TEXT	14 WORDS
<p>Risk Function The financial markets provide protection against life, health and income risks.</p> <p>SA book fm(1).doc (D144076294)</p>					
52/173	SUBMITTED TEXT	12 WORDS	95%	MATCHING TEXT	12 WORDS
<p>financial markets provide protection against life, health and income risks. These</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>					
53/173	SUBMITTED TEXT	24 WORDS	100%	MATCHING TEXT	24 WORDS
<p>The financial markets provide immense opportunities for the investor to hedge himself against or reduce the possible risks involved in various investments. 11.3.5</p> <p>SA book fm(1).doc (D144076294)</p>					

54/173	SUBMITTED TEXT	18 WORDS	100% MATCHING TEXT	18 WORDS		
<p>A financial market can be defined as the market in which financial assets are created or transferred.</p>						
<p>SA book fm(1).doc (D144076294)</p>						
55/173	SUBMITTED TEXT	11 WORDS	95% MATCHING TEXT	11 WORDS		
<p>and/or periodic payment in the form of interest or dividend.</p>						
<p>SA BANK SYSTEM.pdf (D133233577)</p>						
56/173	SUBMITTED TEXT	28 WORDS	66% MATCHING TEXT	28 WORDS		
<table><tr><td>Money Market. Call Money Market The call money market forms a part of the national money market, where day-to- day surplus funds, mostly of banks, are traded.</td><td>MONEY MARKET ? Call money market that part of the national money market where the day to day surplus funds, mostly of banks are traded</td></tr></table>					Money Market. Call Money Market The call money market forms a part of the national money market, where day-to- day surplus funds, mostly of banks, are traded.	MONEY MARKET ? Call money market that part of the national money market where the day to day surplus funds, mostly of banks are traded
Money Market. Call Money Market The call money market forms a part of the national money market, where day-to- day surplus funds, mostly of banks, are traded.	MONEY MARKET ? Call money market that part of the national money market where the day to day surplus funds, mostly of banks are traded					
<p>W http://dimr.edu.in/wp-content/uploads/2020/05/205-Fin-notes.pdf</p>						
57/173	SUBMITTED TEXT	15 WORDS	100% MATCHING TEXT	15 WORDS		
<table><tr><td>are repayable on demand at the option of either the lender or the borrower.</td><td>are repayable on demand at the option of either the lender or the borrower.</td></tr></table>					are repayable on demand at the option of either the lender or the borrower.	are repayable on demand at the option of either the lender or the borrower.
are repayable on demand at the option of either the lender or the borrower.	are repayable on demand at the option of either the lender or the borrower.					
<p>W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0</p>						

58/173	SUBMITTED TEXT	18 WORDS	62% MATCHING TEXT	18 WORDS		
<p>some of the examples of a Money Market. Call Money Market The call money market forms</p> <p>SA Shivani Sharma, final thesis.pdf (D30330450)</p>						
59/173	SUBMITTED TEXT	14 WORDS	88% MATCHING TEXT	14 WORDS		
<p>at the option of either the lender or the borrower. The interest rate</p> <p>SA jaysingh rawat.pdf (D140381824)</p>						
60/173	SUBMITTED TEXT	13 WORDS	83% MATCHING TEXT	13 WORDS		
<p>serves the purpose of equilibrating the short-term liquidity position of banks.</p> <p>SA book fm(1).doc (D144076294)</p>						
61/173	SUBMITTED TEXT	21 WORDS	97% MATCHING TEXT	21 WORDS		
<table><tr><td>highly rated corporate borrowers, to diversify their sources of short-term borrowings and to provide an additional instrument to investors.</td><td>highly rated corporate borrowers to diversify their sources of short-term borrowings and to provide an additional instrument to investors.</td></tr></table> <p>W http://dimr.edu.in/wp-content/uploads/2020/05/205-Fin-notes.pdf</p>					highly rated corporate borrowers, to diversify their sources of short-term borrowings and to provide an additional instrument to investors.	highly rated corporate borrowers to diversify their sources of short-term borrowings and to provide an additional instrument to investors.
highly rated corporate borrowers, to diversify their sources of short-term borrowings and to provide an additional instrument to investors.	highly rated corporate borrowers to diversify their sources of short-term borrowings and to provide an additional instrument to investors.					

62/173	SUBMITTED TEXT	13 WORDS	100%	MATCHING TEXT	13 WORDS
<p>highly rated corporate borrowers, to diversify their sources of short-term borrowings and</p> <p>SA Shivani Sharma, final thesis.pdf (D30330450)</p>					
63/173	SUBMITTED TEXT	26 WORDS	91%	MATCHING TEXT	26 WORDS
<p>provide an additional instrument to investors. Commercial Paper (CP) is an unsecured usance money market instrument issued in the form of a promissory note</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>					
64/173	SUBMITTED TEXT	31 WORDS	100%	MATCHING TEXT	31 WORDS
<p>bodies, Non-Resident Indians (NRIs), and Foreign Institutional Investors (FIIs). However, investment by FIIs would be within the limits set for their investments by Securities and Exchange Board of India (SEBI).</p> <p>SA book fm(1).doc (D144076294)</p>					
65/173	SUBMITTED TEXT	14 WORDS	100%	MATCHING TEXT	14 WORDS
<p>are issued at a discount to the face value and the discount rate</p> <p>W https://fliphtml5.com/xwtao/htyo/basic/251-282</p>					

66/173	SUBMITTED TEXT	36 WORDS	100% MATCHING TEXT	36 WORDS
	Amount Outstanding (₹ Crore) 104705.00 68209.42 69,299.52 64,586.90 64,304.10 1.1 Issued during the fortnight (₹ Crore) 1292.97 6209.13 8817.62 270.74 950.89 2 Rate of Interest (per cent) 3.39-4.45 3.44-4.11 3.44-4.21 3.68-4.21 4.05-4.85		Amount Outstanding (Crore) 225478.45 173941.00 172996.00 180116.00 180891.00 1.1 Issued during the fortnight (Crore) 4582.87 19166.55 18290.30 12556.15 4539.49 2 Rate of Interest (per cent) 6.65-7.33 4.95-6.50 4.96-8.80 4.70-7.94 4.70-7.84	
	W https://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/RBIJUNE20206CD876E1B1344CAA82A8286E6D65F81D.PDF			
67/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
	are issued at a discount to the face value and			
	SA book fm(1).doc (D144076294)			
68/173	SUBMITTED TEXT	12 WORDS	83% MATCHING TEXT	12 WORDS
	long-term instruments through which corporate entities borrow from the capital market.			
	SA 023E2430_Financial Markets and Institutions.pdf (D165201762)			
69/173	SUBMITTED TEXT	28 WORDS	58% MATCHING TEXT	28 WORDS
	Private Placement Bank of India, in September 2021 raised ₹ 1,800 crore by issue of Basel III compliant bonds Tier –II bonds on a private placement basis		private placement basis.of India had earlier raised ₹1,352 crore of Basel-III compliant additional tier-I bonds on a private placement basis.	
	W https://www.livemint.com/industry/banking/bank-of-india-raises-rs-1-800-cr-through-basel-iii-comp...			

70/173	SUBMITTED TEXT	12 WORDS	100% MATCHING TEXT	12 WORDS
	of Basel-III compliant additional tier-I bonds on a private placement basis.		of Basel-III compliant additional tier-I bonds on a private placement basis.	
	W https://www.livemint.com/industry/banking/bank-of-india-raises-rs-1-800-cr-through-basel-iii-comp ...			
71/173	SUBMITTED TEXT	1 WORDS	88% MATCHING TEXT	1 WORDS
	industry/banking/bank-of-india-raises-rs-1-800-cr-through-basel-iii-compliant-bonds-11633006728250.		Industry / Banking / Bank of India raises ₹1,800 cr through Basel-III-compliant bonds	
	W https://www.livemint.com/industry/banking/bank-of-india-raises-rs-1-800-cr-through-basel-iii-comp ...			
72/173	SUBMITTED TEXT	14 WORDS	76% MATCHING TEXT	14 WORDS
	to allow stock exchanges to offer T+1 trade cycle instead of T+2 cycle		to allow stock exchanges the option to offer the faster T+1 trade cycle instead of the existing T+2 cycle	
	W https://www.livemint.com/market/stock-market-news/sebi-to-shorten-trade-settlement-cycle-optional ...			
73/173	SUBMITTED TEXT	12 WORDS	83% MATCHING TEXT	12 WORDS
	long-term instruments through which corporate entities borrow from the capital market.			
	SA Chapter 4 IFS MONEY MARKET final.docx (D156861167)			

74/173	SUBMITTED TEXT	16 WORDS	90% MATCHING TEXT	16 WORDS
<p>is an unsecured usance money market instrument issued in the form of a promissory note</p> <p>is an unsecured money market instrument issued in the form of a promissory note</p> <p>W http://dimr.edu.in/wp-content/uploads/2020/05/205-Fin-notes.pdf</p>				
75/173	SUBMITTED TEXT	16 WORDS	90% MATCHING TEXT	16 WORDS
<p>is an unsecured usance money market instrument issued in the form of a promissory note</p> <p>SA 023E2430_Financial Markets and Institutions.pdf (D165201762)</p>				
76/173	SUBMITTED TEXT	17 WORDS	100% MATCHING TEXT	17 WORDS
<p>a government security is a tradable instrument issued by the Central Government or the State Governments.</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				
77/173	SUBMITTED TEXT	39 WORDS	82% MATCHING TEXT	39 WORDS
<p>original maturities of less than one year. The long-term Government bonds or dated securities have original maturity of one year or more. In India, the Central Government issues both treasury bills and bonds or dated securities 11.6.1</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				

78/173	SUBMITTED TEXT	32 WORDS	48% MATCHING TEXT	32 WORDS
<p>Industrial Development Bank of India (IDBI) Industrial Development Bank of India (IDBI) was established in 1964 as a subsidiary of the Reserve Bank of India by an Act of the Parliament</p> <p>W https://fliphtml5.com/xwtao/htyo/basic/251-282</p>		<p>INDUSTRIAL DEVELOPMENT BANK OF INDIA (IDBI) The Industrial Development Bank of India was set up as wholly owned subsidiary of the RBI on July 1st 1964 under an act of parliament.</p>		
79/173	SUBMITTED TEXT	14 WORDS	88% MATCHING TEXT	14 WORDS
<p>Industrial Development Bank of India (IDBI) Industrial Development Bank of India (IDBI) was</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				
80/173	SUBMITTED TEXT	13 WORDS	100% MATCHING TEXT	13 WORDS
<p>planning, promoting and developing industries to fill the gaps in the industrial</p> <p>SA Shivani Sharma, final thesis.pdf (D30330450)</p>				
81/173	SUBMITTED TEXT	18 WORDS	73% MATCHING TEXT	18 WORDS
<p>Industrial Finance Corporation of India (IFCI) Industrial Finance Corporation of India (IFCI) was the first financial institution</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				

82/173	SUBMITTED TEXT	14 WORDS	76% MATCHING TEXT	14 WORDS
<p>Industrial Finance Corporation of India (IFCI) was the first financial institution to be</p> <p>SA Shivani Sharma, final thesis.pdf (D30330450)</p>				
83/173	SUBMITTED TEXT	12 WORDS	100% MATCHING TEXT	12 WORDS
<p>to Review the arrangements for Institutional Credit for Agriculture and Rural</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				
84/173	SUBMITTED TEXT	14 WORDS	100% MATCHING TEXT	14 WORDS
<p>to Review the arrangements for Institutional Credit for Agriculture and Rural Development (CRAFICARD).</p> <p>SA 023E2430_Financial Markets and Institutions.pdf (D165201762)</p>				
85/173	SUBMITTED TEXT	16 WORDS	71% MATCHING TEXT	16 WORDS
<p>credit functions of RBI and the refinance functions of Agriculture Refinance and Development Corporation.</p> <p>SA 023E2430_Financial Markets and Institutions.pdf (D165201762)</p>				

86/173	SUBMITTED TEXT	11 WORDS	100%	MATCHING TEXT	11 WORDS
<p>for regulating and supervising the functions of co-operative banks and</p> <p>SA 023E2430_Financial Markets and Institutions.pdf (D165201762)</p>					
87/173	SUBMITTED TEXT	11 WORDS	100%	MATCHING TEXT	11 WORDS
<p>for regulating and supervising the functions of co-operative banks and</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>					
88/173	SUBMITTED TEXT	14 WORDS	84%	MATCHING TEXT	14 WORDS
<p>State Cooperative Banks (StCBs), Central Cooperative Banks (DCCBs) and Regional Rural Banks (RRBs).</p> <p>SA 023E2430_Financial Markets and Institutions.pdf (D165201762)</p>					
89/173	SUBMITTED TEXT	15 WORDS	85%	MATCHING TEXT	15 WORDS
<p>of State Cooperative Banks (StCBs), Central Cooperative Banks (DCCBs) and Regional Rural Banks (RRBs).</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>					

90/173	SUBMITTED TEXT	18 WORDS	82% MATCHING TEXT	18 WORDS
<p>to conduct inspection of State Cooperative Banks (StCBs), Central Cooperative Banks (DCCBs) and Regional Rural Banks (RRBs).</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				
91/173	SUBMITTED TEXT	35 WORDS	100% MATCHING TEXT	35 WORDS
<p>In addition, NABARD has also been conducting periodic inspections of state level cooperative institutions such as State Cooperative Agriculture and Rural Development Banks (SCARDBs), Apex Weavers Societies, Marketing Federations etc., on a voluntary basis.</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>				
92/173	SUBMITTED TEXT	11 WORDS	91% MATCHING TEXT	11 WORDS
<p>co-operative banks, housing finance companies, apex co-operative housing finance societies,</p> <p>SA Chapter 4 IFS MONEY MARKET final.docx (D156861167)</p>				
93/173	SUBMITTED TEXT	12 WORDS	100% MATCHING TEXT	12 WORDS
<p>State Industrial Development Corporations (SIDCs) The State Industrial Development Corporations</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				

94/173	SUBMITTED TEXT	15 WORDS	100% MATCHING TEXT	15 WORDS
	Small Industries Development Bank of India (SIDBI) The Small Industries Development Bank of India		Small Industries Development Bank of India (SIDBI) The Small Industries Development Bank of India (
	W https://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/RBIJUNE20206CD876E1B1344CAA82A8286E6D65F81D.PDF			
95/173	SUBMITTED TEXT	16 WORDS	78% MATCHING TEXT	16 WORDS
	State Industrial Development Corporations (SIDCs) The State Industrial Development Corporations have been set up			
	SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)			
96/173	SUBMITTED TEXT	15 WORDS	75% MATCHING TEXT	15 WORDS
	Small Industries Development Bank of India (SIDBI) The Small Industries Development Bank of India			
	SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)			
97/173	SUBMITTED TEXT	29 WORDS	40% MATCHING TEXT	29 WORDS
	Small Industries Development Bank of India was started in April 1990 under an act of Parliament. It is the major financial institution that promotes financing and development of			
	SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)			

98/173	SUBMITTED TEXT	27 WORDS	62% MATCHING TEXT	27 WORDS
<p>April 1990 under an act of Parliament. It is the major financial institution that promotes financing and development of Micro, Small and Medium Enterprises (MSME) sector.</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>				
99/173	SUBMITTED TEXT	16 WORDS	100% MATCHING TEXT	16 WORDS
<p>Functions of Reserve Bank of India The Reserve Bank of India</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				
100/173	SUBMITTED TEXT	32 WORDS	48% MATCHING TEXT	32 WORDS
<p>Reserve Bank of India The Reserve Bank of India is considered as the nerve center of the Indian monetary system. It was established on 1st April, 1935</p> <p>SA book fm(1).doc (D144076294)</p>				
101/173	SUBMITTED TEXT	19 WORDS	91% MATCHING TEXT	19 WORDS
<p>It was established on 1st April, 1935 under the Reserve Bank of India Act. It was a private shareholder'</p> <p>SA Shivani Sharma, final thesis.pdf (D30330450)</p>				

102/173	SUBMITTED TEXT	14 WORDS	80% MATCHING TEXT	14 WORDS
<p>withdraw from it, but also to exchange notes and coins of one denomination</p> <p>SA Chapter 4 IFS MONEY MARKET final.docx (D156861167)</p>				
103/173	SUBMITTED TEXT	12 WORDS	100% MATCHING TEXT	12 WORDS
<p>Bank Rate: It is the rate at which the Reserve Bank</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>				
104/173	SUBMITTED TEXT	21 WORDS	95% MATCHING TEXT	21 WORDS
<p>Policy Repo Rate : 4.00% Reverse Repo Rate : 3.35% Marginal Standing Facility Rate : 4.25% Bank Rate : 4.25%</p> <p>Policy Repo Rate 4.40 4.2 Reverse Repo Rate 4.00 4.3 Marginal Standing Facility (MSF) Rate 4.65 4.4 Bank Rate 4.65 4.5</p> <p>W https://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/RBIJUNE20206CD876E1B1344CAA82A8286E6D65F81D.PDF</p>				
105/173	SUBMITTED TEXT	12 WORDS	100% MATCHING TEXT	12 WORDS
<p>Bank Rate: It is the rate at which the Reserve Bank</p> <p>SA Alrin div-B.pdf (D114718748)</p>				
106/173	SUBMITTED TEXT	21 WORDS	95% MATCHING TEXT	21 WORDS
<p>Policy Repo Rate : 4.00% Reverse Repo Rate : 3.35% Marginal Standing Facility Rate : 4.25% Bank Rate : 4.25%</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				

107/173	SUBMITTED TEXT	20 WORDS	88%	MATCHING TEXT	20 WORDS
<p>To administer the foreign exchange control. ? To choose the exchange rate system and fix or manage the exchange</p> <p>SA Chapter 4 IFS MONEY MARKET final.docx (D156861167)</p>					
108/173	SUBMITTED TEXT	24 WORDS	75%	MATCHING TEXT	24 WORDS
<p>exchange reserves. As the central bank is the custodian of the country's foreign exchange reserves, it is vested with the responsibility of managing</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>					
109/173	SUBMITTED TEXT	79 WORDS	71%	MATCHING TEXT	79 WORDS
<p>is the custodian of the country's foreign exchange reserves, it is vested with the responsibility of managing the investment and utilization of reserves in foreign exchange. The Reserve Bank manages buying and selling of foreign exchange from and to commercial banks (who are authorized dealers in Indian forex markets). The apex bank also manages the investment of reserves in gold accounts abroad and the shares and securities issued by foreign governments and international banks or financial institutions.</p> <p>SA Chapter 4 IFS MONEY MARKET final.docx (D156861167)</p>					

110/173	SUBMITTED TEXT	21 WORDS	87% MATCHING TEXT	21 WORDS
<p>the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly.</p> <p>SA Alrin div-B.pdf (D114718748)</p>				
111/173	SUBMITTED TEXT	21 WORDS	87% MATCHING TEXT	21 WORDS
<p>the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly.</p> <p>SA FINAL SIP Report PDF.pdf (D113834670)</p>				
112/173	SUBMITTED TEXT	39 WORDS	85% MATCHING TEXT	39 WORDS
<p>ALM Information System (Management Information System, Information availability, accuracy, adequacy and expediency) 2. ALM Organization (Structure and responsibilities, Level of top management involvement) 3. ALM Process (Risk parameters, Risk identification, Risk measurement, Risk management,</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				
113/173	SUBMITTED TEXT	14 WORDS	100% MATCHING TEXT	14 WORDS
<p>should be responsible for analyzing, monitoring and reporting the risk profiles to the</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				

114/173	SUBMITTED TEXT	15 WORDS	100% MATCHING TEXT	15 WORDS
<p>of the total voting rights of all the shareholders of the banking company.</p> <p>SA Shivani Sharma, final thesis.pdf (D30330450)</p>				
115/173	SUBMITTED TEXT	13 WORDS	100% MATCHING TEXT	13 WORDS
<p>to observe priority sector lending targets as applicable to other domestic banks</p> <p>SA Shivani Sharma, final thesis.pdf (D30330450)</p>				
116/173	SUBMITTED TEXT	23 WORDS	65% MATCHING TEXT	23 WORDS
<p>a body corporate having perpetual succession and a common seal with power to acquire, hold and dispose of property, and to contract.</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				
117/173	SUBMITTED TEXT	36 WORDS	84% MATCHING TEXT	36 WORDS
<div> <div> Protection of the interests of the policyholders in matters concerning assigning of policy, nomination by policyholders, insurable interest, settlement of insurance claim, surrender value of policy and other terms and conditions of contract of insurance;</div> <div> Protection of the interests of the policy holders in matters concerning assigning of policy, nomination by policy holders, insurable interest, settlement of insurance claim, surrender value of policy and other terms and conditions of contracts of insurance;</div> </div> <p>W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0</p>				

118/173	SUBMITTED TEXT	12 WORDS	100% MATCHING TEXT	12 WORDS
	certificate of registration, renew, modify, withdraw, suspend or cancel such registration;		certificate of registration, renew, modify, withdraw, suspend or cancel such registration;	
	W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0			
119/173	SUBMITTED TEXT	17 WORDS	100% MATCHING TEXT	17 WORDS
	Specifying requisite qualifications, code of conduct and practical training for intermediary or insurance intermediaries and agents;		Specifying requisite qualifications, code of conduct and practical training for intermediary or insurance intermediaries and agents	
	W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0			
120/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
	Specifying the code of conduct for surveyors and loss assessors;		Specifying the code of conduct for surveyors and loss assessors;	
	W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0			
121/173	SUBMITTED TEXT	20 WORDS	84% MATCHING TEXT	20 WORDS
	Promoting efficiency in the conduct of insurance business; f. Promoting and regulating professional organizations connected with the insurance and		Promoting efficiency in the conduct of insurance business; Promoting and regulating professional organisations connected with the insurance and	
	W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0			

122/173	SUBMITTED TEXT	60 WORDS	82% MATCHING TEXT	60 WORDS
<p>Calling for information from, undertaking inspection of, conducting inquiries and investigations, including audit of the insurers, intermediaries, insurance intermediaries and other organizations connected with the insurance business; h. Control and regulation of rates, advantages, terms and conditions that may be offered by insurers in respect of general insurance business not so controlled and regulated by the Tariff Advisory Committee;</p>		<p>Calling for information from, undertaking inspection of, conducting enquiries and investigations including audit of the insurers, intermediaries, insurance intermediaries and other organisations connected with the insurance business; Control and regulation of the rates, advantages, terms and conditions that may be offered by insurers in respect of general insurance business not so controlled and regulated by the tariff advisory committee</p>		
<p>W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0</p>				
123/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
<p>Adjudication of disputes between insurers and intermediaries or insurance intermediaries;</p>		<p>Adjudication of disputes between insurers and intermediaries or insurance intermediaries;</p>		
<p>W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0</p>				
124/173	SUBMITTED TEXT	24 WORDS	100% MATCHING TEXT	24 WORDS
<p>Specifying the percentage of life insurance business and general insurance business to be undertaken by the insurer in the rural or social sector.</p>		<p>Specifying the percentage of life insurance business and general insurance business to be undertaken by the insurer in the rural or social sector;</p>		
<p>W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0</p>				
125/173	SUBMITTED TEXT	12 WORDS	83% MATCHING TEXT	12 WORDS
<p>and ensure orderly growth of the insurance and re-insurance business. The</p>				
<p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				

126/173	SUBMITTED TEXT	16 WORDS	66% MATCHING TEXT	16 WORDS
<p>The sources of their funds are share capital, deposits from their members, and the public.</p> <p>SA Chapter 4 IFS MONEY MARKET final.docx (D156861167)</p>				
127/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
<p>services for a fee, while commercial banks accept deposits and</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				
128/173	SUBMITTED TEXT	25 WORDS	50% MATCHING TEXT	25 WORDS
<p>Hire Purchase Finance Companies Hire purchase involves a system under which term loans for purchases of goods and services are advanced to be liquidated</p> <p>SA Chapter 4 IFS MONEY MARKET final.docx (D156861167)</p>				
129/173	SUBMITTED TEXT	11 WORDS	91% MATCHING TEXT	11 WORDS
<p>co-operative banks, housing finance companies, apex co-operative housing finance societies,</p> <p>SA Chapter 4 IFS MONEY MARKET final.docx (D156861167)</p>				

130/173	SUBMITTED TEXT	13 WORDS	100%	MATCHING TEXT	13 WORDS
<p>is owned and operated for the benefit of its 188 member countries.</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>					
131/173	SUBMITTED TEXT	10 WORDS	100%	MATCHING TEXT	10 WORDS
<p>most of its funds on the world's financial markets</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>					
132/173	SUBMITTED TEXT	16 WORDS	73%	MATCHING TEXT	16 WORDS
<p>The income earned by IBRD over the years has allowed it to fund development activities</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>					
133/173	SUBMITTED TEXT	44 WORDS	87%	MATCHING TEXT	44 WORDS
<p>International Development Association (IDA) The International Development Association (IDA) helps the world's poorest countries. Established in 1960, IDA aims to reduce poverty by providing loans (called "credits") and grants for programs that boost economic growth, reduce inequalities, and improve people's living conditions. IDA</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>					

134/173	SUBMITTED TEXT	82 WORDS	100%	MATCHING TEXT	82 WORDS
<p>IDA is one of the largest sources of assistance for the world's 77 poorest countries, 39 of which are in 19</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>					
135/173	SUBMITTED TEXT	34 WORDS	98%	MATCHING TEXT	34 WORDS
<p>little or no interest and repayments are stretched over 25 to 38 years, including a 5 – 10 year grace period. IDA also provides grants to countries at risk of debt distress. 11.14</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>					
136/173	SUBMITTED TEXT	11 WORDS	100%	MATCHING TEXT	11 WORDS
<p>CD) is a negotiable promissory note, secure and short term</p> <p>SA Alrin div-B.pdf (D114718748)</p>					
137/173	SUBMITTED TEXT	11 WORDS	100%	MATCHING TEXT	11 WORDS
<p>CD) is a negotiable promissory note, secure and short term</p> <p>SA FINAL SIP Report PDF.pdf (D113834670)</p>					
138/173	SUBMITTED TEXT	13 WORDS	95%	MATCHING TEXT	13 WORDS
<p>are issued at a discount to the face value, the discount rate</p> <p>W https://fliphtml5.com/xwtao/htyo/basic/251-282</p>					

139/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
are issued at a discount to the face value, the				
SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)				
140/173	SUBMITTED TEXT	12 WORDS	95% MATCHING TEXT	12 WORDS
interest paid on call loans is known as the call rate.				
SA jaysingh rawat.pdf (D140381824)				
141/173	SUBMITTED TEXT	2 WORDS	100% MATCHING TEXT	2 WORDS
scouting-for-a-private-equity-partner-the-case- of-tata-motors/		Scouting for a Private Equity Partner- The Case of Tata Motors		
W https://icfaibytes.in/2021/09/02/bajaj-finance-surpasses-sbi-in-market-cap/				
142/173	SUBMITTED TEXT	15 WORDS	78% MATCHING TEXT	15 WORDS
to the public in the primary market and get them listed on the stock		to the public in the primary market and/ or listed on the Stock		
W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0				

143/173	SUBMITTED TEXT	72 WORDS	100%	MATCHING TEXT	72 WORDS
$ \begin{aligned} & \times 0.10) = 1100 \quad 1000 + (1000 \times 0.10) = 1100 \quad 2 \quad 1100 + (1100 \times \\ & 0.10) = 1210 \quad 1100 + (1000 \times 0.10) = 1200 \quad 3 \quad 1210 + (1210 \times 0.10) \\ & = 1331 \quad 1200 + (1000 \times 0.10) = 1300 \quad 4 \quad 1331 + (1331 \times 0.10) = \\ & 1464 \quad 1300 + (1000 \times 0.10) = 1400 \quad 5 \quad 1464 + (1464 \times 0.10) = \\ & 1610 \quad 1400 + (1000 \times 0.10) = 1500 \end{aligned} $					
SA book fm(1).doc (D144076294)					
144/173	SUBMITTED TEXT	14 WORDS	100%	MATCHING TEXT	14 WORDS
Check Your Progress – 1 1. Which of the following is not a					
SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)					
145/173	SUBMITTED TEXT	16 WORDS	100%	MATCHING TEXT	16 WORDS
issued by the Reserve Bank of India (RBI) on behalf of the Government of India.					
SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)					
146/173	SUBMITTED TEXT	16 WORDS	65%	MATCHING TEXT	16 WORDS
Reserve Bank of India (RBI) on behalf of the Government of India. T-bills are issued					
SA Chapter 4 IFS MONEY MARKET final.docx (D156861167)					

147/173	SUBMITTED TEXT	15 WORDS	71% MATCHING TEXT	15 WORDS
<p>The Reserve Bank of India acts as a banker to the Government of India.</p> <p>SA Major Project Report_07416688519.docx (D110634119)</p>				
148/173	SUBMITTED TEXT	14 WORDS	85% MATCHING TEXT	14 WORDS
<p>generally up to one year. Thus, they are useful in managing short-term liquidity.</p> <p>W http://dimr.edu.in/wp-content/uploads/2020/05/205-Fin-notes.pdf</p> <p>generally up to one year. ? They are thus useful in managing short-term liquidity. ?</p>				
149/173	SUBMITTED TEXT	21 WORDS	94% MATCHING TEXT	21 WORDS
<p>Bids for treasury bills are to be made for a minimum amount of ` 25,000 and in multiples thereof.</p> <p>SA Shivani Sharma, final thesis.pdf (D30330450)</p>				
150/173	SUBMITTED TEXT	45 WORDS	100% MATCHING TEXT	45 WORDS
<p>Amount Outstanding (₹ crore) 374817.20 404804.90 376117.85 471218.00 414981.65 1.1 Reported during the fortnight (₹ crore) 53608.10 73440.40 97928.00 117197.20 149052.15 2. Rate of interest (per cent) 3.18-12.33 3.36-11.32 3.43-13.03 3.32-12.80 3.38-12.94</p> <p>Amount Outstanding (Crore) 542885.80 401724.55 344526.95 381273.50 417227.05 1.1 Reported during the fortnight (Crore) 71210.80 148273.30 63166.10 54770.55 77889.20 2 Rate of Interest (per cent) 6.67-13.14 5.01-13.95 4.88-12.39 4.55-9.90 3.78-10.45 ``</p> <p>W https://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/RBIJUNE20206CD876E1B1344CAA82A8286E6D65F81D.PDF</p>				

151/173	SUBMITTED TEXT	13 WORDS	80% MATCHING TEXT	13 WORDS
<p>Transparency in operations as the transactions would be put through RBI's SGL</p> <p>SA Shivani Sharma, final thesis.pdf (D30330450)</p>				
152/173	SUBMITTED TEXT	54 WORDS	96% MATCHING TEXT	54 WORDS
<p>Section 5 of the Negotiable Instruments Act, 1881, defines Bills of Exchange as 'an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument.'</p> <p>SA Alrin div-B.pdf (D114718748)</p>				
153/173	SUBMITTED TEXT	54 WORDS	96% MATCHING TEXT	54 WORDS
<p>Section 5 of the Negotiable Instruments Act, 1881, defines Bills of Exchange as 'an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument.'</p> <p>SA FINAL SIP Report PDF.pdf (D113834670)</p>				

154/173	SUBMITTED TEXT	41 WORDS	100%	MATCHING TEXT	41 WORDS
<p>an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument.</p> <p>SA Alrin div-B.pdf (D114718748)</p>					
155/173	SUBMITTED TEXT	49 WORDS	90%	MATCHING TEXT	49 WORDS
<p>is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument. Identify the instrument. a. Bill of Exchange</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>					
156/173	SUBMITTED TEXT	49 WORDS	93%	MATCHING TEXT	49 WORDS
<p>Bill of exchange is defined as an instrument in writing, containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument. 10. (</p> <p>SA 003_Banking and Indian financial _16-7-13.pdf (D142522847)</p>					

157/173	SUBMITTED TEXT	27 WORDS	70% MATCHING TEXT	27 WORDS
	are as follows: ? Prepare guidelines and rules for forex business ? Train bank personnel in the areas of foreign exchange business ? Provide accreditation		are as follows: 1. Formulations of FEDAI guidelines and FEDAI rules for Forex business. 2. Training of bank personnel in the areas of Foreign Exchange Business. 3. Accreditation	
	W https://docshare.tips/risk-management-in-international-trade-finance_5753febfb6d87f8d958b4607.html			
158/173	SUBMITTED TEXT	32 WORDS	73% MATCHING TEXT	32 WORDS
	forex brokers ? Advise/assist member banks in settling issues/matters in their dealings ? Represent member banks on government/Reserve Bank of India/other bodies ? Announce daily and periodical rates to member banks		Forex Brokers. 4. Advising/Assisting member banks in settling issues/matters in their dealings. 5. Represent member banks on Government/Reserve Bank of India and other bodies. 6. Rules of FEDAI also include announcement of daily and periodical rates to its member banks.	
	W https://docshare.tips/risk-management-in-international-trade-finance_5753febfb6d87f8d958b4607.html			
159/173	SUBMITTED TEXT	44 WORDS	100% MATCHING TEXT	44 WORDS
	as an instrument in writing, containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument. 10. (
	SA Alrin div-B.pdf (D114718748)			
160/173	SUBMITTED TEXT	15 WORDS	71% MATCHING TEXT	15 WORDS
	RBI, other organizations like FIMMDA, the Forex Association of India and various market participants.		RBI), other organizations like Fixed Income Money Market and Derivatives Association (FIMMDA), the Forex Association of India and various other market participants. 31	
	W https://docshare.tips/risk-management-in-international-trade-finance_5753febfb6d87f8d958b4607.html			

161/173	SUBMITTED TEXT	24 WORDS	93% MATCHING TEXT	24 WORDS
<p>guidelines in the name of Uniform Customs and Practice for Documentary Credits (UCPDC) to provide uniform interpretation of terminology used under documentary credit.</p>		<p>guidelines in the name of Uniform Customs and Practice for Documentary Credits (UCPDC) to facilitate uniform interpretation of terminology used under documentary credit</p>		
<p>W https://docshare.tips/risk-management-in-international-trade-finance_5753febf6d87f8d958b4607.html</p>				

162/173	SUBMITTED TEXT	51 WORDS	40% MATCHING TEXT	51 WORDS
<p>as any loan or advance granted or any other credit provided by an institution to an exporter from India. This form of finance is provided from the date of extending the credit after shipment of goods to the date of realization of the export proceeds. Different types of post-shipment finance</p>		<p>as "any loan or advance granted or any credit provided by a bank to an exporter of goods from India from the date extending the credit after shipment of the goods to the date of realization of the export proceeds." FEATURES OF POST-SHIPMENT FINANCE:</p>		
<p>W https://docshare.tips/risk-management-in-international-trade-finance_5753febf6d87f8d958b4607.html</p>				

163/173	SUBMITTED TEXT	137 WORDS	89% MATCHING TEXT	137 WORDS
<p>Foreign Exchange Dealers Association of India (FEDAI) was set up in 1958 as an association of banks dealing in foreign exchange in India (typically called Authorised Dealers —ADs) as a self-regulatory body and is incorporated under Section 25 of The Companies Act, 1956. Its major activities include framing of rules governing the conduct of inter-bank foreign exchange business among banks vis-à-vis public and liaison with RBI for reforms and development of forex market. Presently some of the functions are as follows: ? Prepare guidelines and rules for forex business ? Train bank personnel in the areas of foreign exchange business ? Provide accreditation to forex brokers ? Advise/assist member banks in settling issues/matters in their dealings ? Represent member banks on government/Reserve Bank of India/other bodies ? Announce daily and periodical rates to member banks</p>				
<p>SA Summer Internship_Yamini Kalwani_249.doc (D21543163)</p>				

164/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
<p>orderly development and maintenance of foreign exchange market in India.</p>				
<p>W http://dimr.edu.in/wp-content/uploads/2020/05/205-Fin-notes.pdf</p>				

165/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
<p>orderly development and maintenance of foreign exchange market in India.</p>				
<p>W https://zdocs.tips/doc/5th-term-financial-services-markets-3d1mn53qx9p0</p>				

166/173	SUBMITTED TEXT	25 WORDS	81% MATCHING TEXT	25 WORDS
<p>and amend the law relating to foreign exchange with the objective of facilitating external trade and payments and for promoting the orderly development and</p> <p>SA FMG-302 Indian Financial System and Management of Financial Institutions.pdf (D164737022)</p>				
167/173	SUBMITTED TEXT	13 WORDS	83% MATCHING TEXT	13 WORDS
<p>Service Exports from India Scheme (SEIS) Service Exports from India Scheme is</p> <p>W https://www.ibef.org/blogs/indian-export-incentive-schemes</p> <p>Service Exports from India Scheme (SEIS) The objective of 'Service Exports from India Scheme' (SEIS) is</p>				
168/173	SUBMITTED TEXT	11 WORDS	100% MATCHING TEXT	11 WORDS
<p>orderly development and maintenance of foreign exchange market in India.</p> <p>SA mangal . Intoduction to Financial Markets & Institutions& Project- Student.docx (D22478819)</p>				
169/173	SUBMITTED TEXT	27 WORDS	100% MATCHING TEXT	27 WORDS
<p>One Star Export House 3 Two Star Export House 25 Three Star Export House 100 Four Star Export House 500 Five Star Export House 2000</p> <p>SA JSNR_SSOU_BBA_Global Banking & Finance_Final_Text 188.pdf (D27249834)</p>				

170/173	SUBMITTED TEXT	45 WORDS	98% MATCHING TEXT	45 WORDS
<p>Foreign Exchange Dealers Association of India (FEDAI) was set up in 1958 as an association of banks dealing in foreign exchange in India (typically called Authorised Dealers —ADs) as a self-regulatory body and is incorporated under Section 25 of The Companies Act, 1956. ?</p> <p>SA Summer Internship_Yamini Kalwani_249.doc (D21543163)</p>				
171/173	SUBMITTED TEXT	15 WORDS	96% MATCHING TEXT	15 WORDS
<p>international trade. International Trade is the exchange of goods and services across international boundaries.</p> <p>International trade. International Trade is the exchange of capital, goods and services across international boundaries</p> <p>W https://docshare.tips/risk-management-in-international-trade-finance_5753febf6d87f8d958b4607.html</p>				
172/173	SUBMITTED TEXT	20 WORDS	71% MATCHING TEXT	20 WORDS
<p>as any loan or advance granted or any other credit provided by an institution to an exporter from India.</p> <p>as "any loan or advance granted or any credit provided by a bank to an exporter of goods from India</p> <p>W https://docshare.tips/risk-management-in-international-trade-finance_5753febf6d87f8d958b4607.html</p>				
173/173	SUBMITTED TEXT	58 WORDS	76% MATCHING TEXT	58 WORDS
<p>FEDAI set up in 1958 is an association of banks dealing in foreign exchange in India (typically called Authorised Dealers —ADs). It is a self-regulatory body and its major activities include framing of rules governing the conduct of inter- bank foreign exchange business among banks vis-à-vis public and liaison with RBI for reforms and development of forex market.</p> <p>SA Summer Internship_Yamini Kalwani_249.doc (D21543163)</p>				

