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M. Com. Part-II

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Preface

It gives us immense pleasure to place the Self Instructional Material (SIM) of Business Finance (Paper I & II). This book has been written keeping in mind the requirement of the students of distance education. However, it may be helpful to teachers also.

The text of this book has been divided into four chapters for Semester IV. The first unit emphasizes on Capital Markets. The second unit covers Mutual Funds, Portfolio Management and Micro Finance. The unit number three includes Corporate Restructuring and while fourth unit emphasizes on Financial Decision making.

The book has been written keeping in mind 'teach yourself' technique. The language used is lucid and objective type questions; short notes as well as long answer questions are given at the end of each unit for self-study and practice.

We are thankful to the authors who have contributed significantly in this book. We are also thankful to Director, Distance Education and office bears of the university as well as distance education center for facilitating this book to the readers.We hope that this book will prove to be useful to students at M.Com. Part II Sem. IV as well as teachers.We also appeal that if there are any suggestions; please let us know so that this can be further improved.

■ **Editors** ■

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Business Finance
M. Com. II Semester-IV

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M. Com Part-II

Semester IV

BUSINESS FINANCE PAPER II

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Each Unit begins with the section 'Objectives' -

Objectives are directive and indicative of :

1. What has been presented in the Unit and
2. What is expected from you
3. What you are expected to know pertaining to the specific Unit once you have completed working on the Unit.

The self check exercises with possible answers will help you to understand the Unit in the right perspective. Go through the possible answer only after you write your answers. These exercises are not to be submitted to us for evaluation. These are provided to you as Study Tools to help keep you in the right track as you study the Unit.

Unit-1

Indian Capital Markets

Unit Structure

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1.0 Objectives:

After studying this unit, the students will be able to:

- Understand the concept of Indian Capital Markets
- Study the meaning and functions of primary capital market and its methods of selling corporate securities.
- Know the underwriting of securities and Greenshoe Option and IPO V/s FPO.
- Understand the Meaning and functions of Secondary Capital Market (Stock Exchange) with online trading procedure on a stock exchange
- Know the role of SEBI in regulating capital market in India

- Understand the meaning and need of Credit Rating with credit rating agencies in India and its methodology
- Study the concept and benefits of Depository Services and its position in India.
- Learn the concept of NSDL and CDSL.
- Understand the concept and importance of Mutual Funds and its types with objectives of AMFI.

1.1 Introduction:

Any individual saves out of their current income to meet future requirements of fund for different purposes. When the amount saved is small, the individual may keep it in the form of cash with himself. But as the savings increases, he/she may invest in banks to earn more rate of interest, or contribute to a provident fund account. Further if the savings are substantial he/she may think of investing in physical assets or financial assets. Investing in physical assets refer to investing the surplus funds in land, building, gold, silver, precious stones etc. Investment in financial assets means investing the surplus funds in financial securities such as shares, bonds and debentures, saving certificates, fixed deposits etc. While investing the surplus or savings an individual investor always considers five important factors. They are safety, liquidity, yield, tax benefit and the convenience. Safety refers to minimum risk of losing the money invested, liquidity refers to ease in converting physical or financial assets into ready cash, yield refers to the rate of return on investment made. Tax benefit refers to the getting some tax relief benefit which accrues to the investors when investment is made in certain securities and convenience refers to ease with which surplus can be invested, marketed and accounted. Though investment in physical assets offer highest safety to the investment, financial assets offer better liquidity and also yield. The investor who wants to invest in financial assets can purchase the asset from the capital market.

Capital market is one of the significant aspects of every financial market. Broadly speaking the capital market is a market for financial assets which have a long or indefinite maturity. Unlike money market instruments, the capital market instruments become mature for the period above one year. It is an institutional arrangement to borrow and lend money for a longer period of time. Business units and corporate are the borrowers in the capital market. It involves various instruments which can be used for financial transactions. It provides long term debt and equity finance for the government and the corporate sector. This unit cover the Indian capital market comprising primary and secondary market with credit rating and depository services.

1.2 Presentation of Subject Matter:

1.2.1 Indian Capital Market

The Indian capital market is one of the most important capital markets in the world. It is because; the rate of Indian capital market is growing fast, along with the rapid rate of India's economic growth. It helps to make the capital market more efficient and inclusive. It is an important component of the country's financial system, playing a considerable role in mobilizing, savings and channeling them toward productive investments. It provides a platform for corporations to raise funds from investors and the public for facilitating economic growth and development. It evolved the way of market operates the asset classes, the structure of the exchanges, and more, over the time. As per the convenience of the investors and market participants, the adjustments have been implemented progressively. The authority of securities regulatory throughout the world have monitoring mechanisms for mitigating such acts in order to prevent market participants to take undue advantage of the information. In the past few decades of liberalization, privatization, and globalization, the Indian capital market has witnessed significant growth. The market has also been happy by a growing middle class with a greater propensity to invest in financial assets, increasing investor awareness and education, and the development of technology-enabled platforms for trading and investing.

1.2.2 Concept and Structure

India capital market is a financial market where long-term debt or equity-backed securities are bought and sold. Suppliers are people/organizations with the capital to lend or invest. Banks and investors are common examples. Securities Exchange Board of India (SEBI) governs the capital market in India. The term capital market can defined as *"A series of channels through which savings of the community are made available to industrial and commercial enterprises and public authorities"* Indian capital markets are defined as markets in which money is provided for longer periods. It is a channel the wealth of savers to those who can put it to long-term productive use, such as companies or governments making long-term investments. It has more clear the concept of Capital Market with following definitions.

According to ***Herbert E. Dougall***, *"Capital Markets are complex of institutions and mechanisms whereby intermediate term funds (Loans upto 10 years maturity) and long term funds (longer maturity loans and corporate stocks) are pooled and made available to business, government and individuals and where instruments that are already outstanding are transferred."*

The features of capital market includes: It is a market where mid and long term securities are traded. It offers higher returns on investment. These markets are not highly liquid in nature but individuals and institutions both participate in the capital market for trading in securities. The Indian capital market provides the support to the system of capitalism of the country. The SEBI and RBI are the two regulatory authorities for Indian securities market, to protect investors and improve the microstructure of capital markets in India. With the increased application of information technology, the trading platforms of stock exchanges are accessible from anywhere in the country through their trading terminals

Structure of Capital Market in India:

Funds Raisers: the Company that raises funds from both public and private resources are called fund raiser.

Fund Providers: These entities can invest funds in the capital markets which are classified as domestic and foreign investors and institutional and retail investors. It includes subscribers to primary market issues, the investors who buy shares and other securities in the secondary market, traders, speculators, mutual funds, investors, venture capital funds, NRIs, etc.

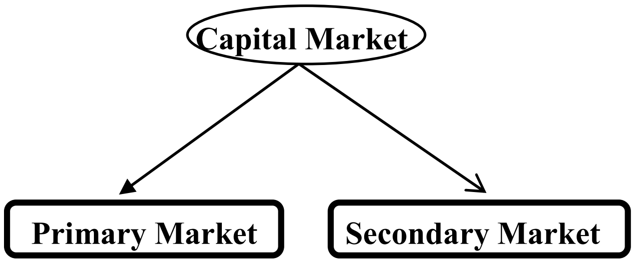
Intermediaries: They provide various services in the market. It includes: stock brokers, sub-brokers, merchant bankers, financiers, underwriters, registrar and transfer agents, depository participants, FIIs/ sub-accounts, venture capital funds, mutual funds, portfolio managers, custodians, etc.

Organizations: Various organizations are participating in capital markets such as, BSE, NSE, other regional stock exchanges etc. In addition to these the two depositories, CSDL and NSDL are also organizations related to capital markets.

Market Regulators: It includes the Department of Company Affairs (DCA), SEBI and RBI.

Thus, the Indian capital market has come a long way in terms of growth and development, driven by various factors, including economic liberalization, techno-advancements and investor awareness. As the Indian economy is growing and it has a good share of the world economy, Indian capital markets are of interest to investors from around the globe. The market has also faced several challenges, which need to be addressed to ensure the continuous growth and development of the Indian capital market. In the future, Indian capital market looks promising, with a range of initiatives and reforming to improve its functioning and make it more robust and efficient.

In India, the capital market comprises two major segments, namely the primary market and the secondary market. The primary market is where corporations issue new securities, such as stocks, bonds, and other financial instruments, to raise capital. Whereas the secondary market, is where existing securities are traded between investors. It shows as under:



1.3. (A) Primary Capital Market

The primary market is the part of the capital market that deals with issuing of new securities. This market creates long term instruments through which corporate entities raise funds from the capital market. The investor purchases the new securities via an investment bank or lead bank or merchant bankers. Primary market also includes the offer of securities to the shareholders by an existing company. In primary market, new issues may be made in three ways namely public issue, right issue and private placement. Public issue refers to sale of securities to the members of the public. Right issue means sale of securities to existing shareholders or debentures holders. Private placement involves selling securities privately to some selected group of investors. In a primary market, companies, governments or public sector institutions can raise funds through bond issues and corporations can raise capital through the sale of new stock through an initial public offering (IPO). This is often done through an investment bank or finance syndicate of securities dealers. The process of selling new shares to investors is called underwriting. Dealers earn a commission that is built into the price of the security offering, though it can be found in the prospectus.

(A).1 Meaning: Primary Capital Market

The primary market is the market where the securities are sold for the first time. This market consists of the companies making the fresh issue of securities and the members of the public subscribing to them. It is also called the new issue market (NIM). The primary market consists of new issues of capital (equity, debenture, bonds etc) by new or existing companies.

Features of primary markets:

1. Primary market is the market for new long term equity capital.
2. The primary market performs the crucial function of facilitating capital formation in the economy.
3. The securities are issued by the company directly to investors.
4. The company receives the money and issues new security certificates to the investors.
5. Primary issues are used by companies for the purpose of beginning new business or for expanding or modernizing the existing business.
6. The new issue market does not include certain other sources of new long term external finance, such as loans from financial institutions.

(A).2 Functions of Primary Capital Market

The main functions of primary capital market are given below:

1. **Organization of New Issues:** After investigation of viability of new projects the organization of new issues possible. It is an important element to know the structure of financial arrangements while organization of new shares. The structure of financial arrangements includes requirements and availability of

promoter's equity, debt-equity ratio, equity from public, short term funds, liquidity ratio etc.

2. **Underwriting of New Issues:** Underwriting is the next step involved in floating of new issue. Underwriting is a guaranteeing purchase of a specified amount of new issue at a fixed price. The purchase may be for sale to the public, for only one's portfolio or for both purposes. Commission paid to underwriter for underwriting the new issue. Mostly underwriting of a new issue is undertaken by a group of financial institutions.

3. **Distribution of New Issue:** The sale of stock to the public is nothing but distribution of new issues. There are three ways of selling the new issue.

   (i) Issue of a Prospectus to the Public- Prospectus is an invitation to the public to purchase the issue. The issue of a public prospectus is done through advertisement. It gives information about the company, issue and the underwriters.

      (a) It Provides Liquidity: Liquidity means an assets easily convertibility into cash shortly with minimum loss of capital value. It helps to develop continuous market for securities, to buy and sell at any time during business hours at small transaction cost.

      (b) Providing liquidity to old stocks: For attracting new finance and for encouraging prospective investors to invest in securities.

   (ii) Encourage New Investment- This market acts as an important indicator of the investment climate in the economy. When prices of existing securities are rising and the volume of trading activity in the secondary market goes up, new issues also tend to increase as the primary market is better preferred. Hence, it is a good time for companies to come forward with new issues

(A). 3 Methods of selling Corporate Securities in Primary Capital Market

The major methods of selling/issuing corporate securities are as under:

1. **Initial Public Offer:**

It is a common method of direct selling new issues of securities. This method enables a company to raise funds from a large number of investors scattered throughout the country. Under this method, the company issues a prospectus to the public inviting offers for subscription. The interested investors willingly apply for the securities to buy. This method ensures a wider distribution of securities thereby leading to diffusion of ownership and avoids concentration of economic power in a few hands. In short, it is suitable method for reputed companies which want to raise large capital and can bear the large costs of a public issue.

2. Private Placement:

Private placement is very suitable, convenient method for small issues particularly during depression. Under this method, the issuing company sells its securities privately to one or more institutional brokers who in turn sell them to their clients and associates. Moreover, the company gets the money quickly and there is no risk of non-receipt of minimum subscription. However it has some drawbacks that, institutional brokers insist a huge discount or other conditions for private purchase of securities. Secondly, it may not sell the securities in the market but keep them with it.

3. Offer for Sale:

Under this method, the issuing company allots the security to an issue house at an agreed price. It saves the company from the cost and trouble of selling securities directly to the investing public. The issue house or financial institution publishes a document called an 'offer for sale'. It offers to the public shares or debentures for sale at higher price. After receiving applications, the issue house renounces the allotment in favour of the applicants who become direct allottees of the shares or debentures.

4. Sale through Intermediaries:

In this process, company appoints intermediaries like stock brokers, commercial banks and financial institutions to assist in marketing for the new securities on commission basis. The company provides blank application forms to every mediator who affixes his seal on them and distributes among proposed investors. Each mediator gets commission on the amount of security applications bearing his seal. However, mediators do not guarantee the sale of securities. But this method saves the administrative problems and expenses involved in direct selling of securities to the public.

5. **Sale through Managing Brokers:**

Sale of securities through managing brokers is more popular method among new companies. Managing brokers advise companies about the terms and conditions as well as proper timing to the issue of securities. They assist companies in pre-issue publicity and issue of prospectus and getting stock exchange listing. They also enlist the support and cooperation of share brokers.

6. **Privileged Subscriptions:**

Under this method, when an existing company wants to issue further securities, it is required to offer them to existing shareholders on prorate basis. It is known as 'Rights Issue'. Sale of shares by rights issues is cheaper as compared to sale through prospectus. But the existing shareholders will subscribe to the new issues only when the past performance and future prospects of the company are good.

7. **Sale to Inside Coterie:**

A company may resort to subscription by promoters and directors. This method helps to save the expenses of public issue. Generally, a percentage of new issue of securities is reserved for subscription by the internal group of people who can in this way share the future prosperity of the company.

Practical work:

1. *List the physical and financial assets for investing the surplus fund as per the safety, liquidity, yield, tax benefit and convenience.*
2. *Visit to any one of the investment bank / lead bank /merchant bankers / stock brokers and fill the following chart, after knowing the monthly or quarterly primary market position, with fresh or new issue by the way of public issue, right issue and private placement.*

Name of Company	**Monthly/Quarterly fresh Issue**								
	Public Issue			***Right Issue***			***Private Placement***		
	Equity	*Debenture*	*Bonds*	*Equity*	*Debenture*	*Bonds*	*Equity*	*Debenture*	*Bonds*

(A).4 Underwriting of Securities:

It is the process by which investment banks raise investment capital from investors on behalf of corporations and governments that are issuing securities (both equity and debt capital). The services of an underwriter are typically used during a public offering in a primary market. Underwriting is the process that a lender or other financial service uses to assess the credit worthiness or risk of a potential customer. These services are provided by some financial institutions, such as banks, insurance or investment houses, whereby they guarantee payment in case of damage or financial loss and accept the financial risk for liability arising from such guarantee. An underwriting arrangement may be created in a number of situations including insurance, issue of securities in primary markets, and in bank lending, among others.

The underwriting standards in place help to set benchmarks for how much debt may be issued to a person, the terms of the loans, how much debt a specific company is willing to issue, and what interest rates will be charged. A securities underwriter or investment bank is the entity that helps corporation raise money from investors. Most of the companies are not set up to manage the sale and then disbursal of many of their investment securities. Selling stocks, bonds or other securities is also an expensive proposition and companies frequently look for ways to reduce costs as well as their risks when doing so. A securities underwriter relieves a client corporation of much of the risk attached to selling its securities. This is a way of distributing a newly issued security, such as stocks or bonds to investors. A lead banks manager underwrites the transaction, which means they have taken on the risk of distributing the securities. Should they not be able to find enough investors, they will have to hold some securities themselves. Underwriters make their income from the price difference (the underwriting spread) between the price they pay the issuer and what they collect from investors or from broker-dealers who buy portions of the offering.

Practical work:

1. *Search and visit the website of listed companies or any broking agencies or its consultant to understanding the procedure / methods to buy the securities of IPO (Initial Public Offer) for investment.*

2. *Discuss with the underwriting service agencies to assess the credit worthiness or risk of a potential customer and understand the role of underwriting securities for raising investment capital from investors on behalf of corporations or Government by issuing securities (both equity and debt capital)*

(A). 5 Greenshoe Option:

Over-allotment options are known as greenshoe option, because in 1919, Green Shoe Manufacturing Company (now called Stride Rite) was the first to issue this type of option. A greenshoe option provides additional price stability to a security issue because the underwriter can increase supply and smooth out price fluctuations. In other word, in the context of an initial public offering (IPO), it is a provision in an underwriting agreement that grants the underwriter the right to sell investors more shares than initially planned by the issuer if the demand for a security issue proves higher than expected. The legal name is "overallotment option" because additional shares are set aside for the underwriters in addition to the shares intended to be offered. SEBI just introduced the greenshoe share option to Indian markets in 2003. Greenshoe options typically allow underwriters to sell up to 15% more shares than the original issue amount. For e.g., if a company instructs the underwriters to sell 200 million shares, the underwriters can issue if an additional 30 million shares by exercising a greenshoe option (200 million shares x 15%). Since underwriters receive their commission as a percentage of the IPO, they have the incentive to make it as large as possible. It has provides price stability and liquidity. Greenshoe options provide buying power to cover short positions if prices fall, without the risk of having to buy shares if the price rises. The greenshoe option benefits not only the company, but also the underwriters, the markets, the investors and the economy. The option allows companies to raise capital and go public with a greater confidence, knowing that they have a mechanism in place to address the increased demand. This increases investor confidence and can lead to greater investment in the company. Additionally, underwriters can use the option to reduce the risk of losing money by buying back shares and stabilizing the price in case of excess demand. This makes the offering more attractive to potential investors and can lead to greater participation in the offering. The greenshoe option gives the underwriters the right to issue and sell more shares than originally planned by the issuer. This can provide additional funds for the issuer and additional profits for the underwriters. Underwriters use greenshoe options in one of two ways. First, if the IPO is a success and the share price surges, the underwriters exercise the option, buy the extra stock from the company at the predetermined price, and issue those shares, at a profit, to their clients. Conversely, if the price starts to fall, they buy back the shares from the market instead of the company to cover their short position, supporting the stock to stabilize its price.

Need of Greenshoe Option: It is an important tool for companies to ensure the success of their IPOs. So the need of greenshoe option as under:

(a) Risk Management: Greenshoe options can help to mitigate the risk for underwriters. By providing a way to stabilize the stock price, it reduces the risk of underwriters being left with unsold shares, which could result in significant losses.

(b) Price Stabilization: It provides price stabilization for newly issued stocks. By allowing underwriters to purchase additional shares and sell them to the market, it helps to maintain the stock price and prevent it from dropping too quickly.

(c) Increased Demand: The additional shares that can be issued through the greenshoe option. It helps to meet increased demand for the stock. This can be especially important in cases where the demand for the stock exceeds the number of shares initially offered.

(d) Flexibility: It provides flexibility to underwriters in managing their positions. They can use the option to cover any short position that they may have taken during the IPO process.

Guidelines for greenshoe option process:

1. Determine the need for a greenshoe option.
2. Incorporate the greenshoe option into the underwriting agreement.
3. File the prospectus with the Securities and Exchange Commission.
4. Conduct the IPO.
5. Determine the need for exercising the greenshoe option.
6. Exercise the greenshoe option.
7. Cover the short position.

Thus, the greenshoe option helps to provide price stability to a security issue by allowing the investment bank to increase the supply of shares if there is high demand and buy back shares if the demand is low.

(A). 6 IPO V/s FPO

Generally capital is an indispensable part of every business. Companies are needed necessary Capital/fund constantly for their establishment, operations, expansion activities, pay off debt etc. There are two basic fundamental ways a company raises fund from the equity market. i.e., Initial Public Offerings (IPO) and Follow on Public Offerings (FPO). Many investors investing in stock markets are confused between IPOs and FPOs. They consider them to be the same. However, that is not true. IPO and FPO are entirely different in various aspects, such as the objective, the risk involved, the status of the issuing company and others. Every beginner who is looking to invest in IPO must have a basic knowledge about these two fundamentals that are widely used in the stock market. So investor in the stock market should be aware of the differences in IPO and FPO for making wise decisions. Before the understanding an actual difference between IPO and FPO, let us know the both concept first. An IPO is a process through which a company offers its shares to the public for the first time. However, a FPO is a procedure for companies to raise funds after it has raised an IPO. There are three major factors that help to understand the difference between IPO and FPO.

1. ***Objective:*** The objective of an IPO is to raise capital from investors by selling its shares to the general public to grow and expand its business. Once the company has done its IPO and achieved the goal of growing their business, they may need additional funds, and that's where FPOs are issued for a company. The primary objective of a company to issue FPO is to expand its equity base. However, FPO can also be used to reduce the shareholdings of a promoter.
2. ***Performance:*** Performance is a main difference between FPO and IPO because it tells how much knowledge or information an investor knows about a company before buying allotted shares. In IPO, investors do not have any major guidance or track record about a company in which they are investing. In FPO, investors know essential information about a company along with a track record of the company's performance after an IPO. However, investors get a signal of whether the stocks are worth investing in or not through sales of equity stakes.

3. ***Profitability:*** IPO can give higher returns for an investor and turn out to be a profitable one than FPOs because investors take part in the starting growth of the company. FPOs tend to have less risk than IPOs since all the information has been available to the investor about the company. FPOs are less profitable than IPOs because, at this stage, the company is in the stabilization phase.

Similarly, in addition to above differences, the following table shows a good idea of the differences between an IPO and an FPO.

Table No.1: IPO V/s FPO

SN	***Particulars***	***IPO***	***FPO***
1	Meaning	IPO is the process through which a company issues its shares to the public for the first time.	Any subsequent issue of shares to the public after an IPO is termed an FPO.
2	Status of the company	An unlisted company issues an IPO	An already-listed company issues an FPO
3	Pricing	Fixed or variable price range	Price is market driven and dependent on the number of shares increasing or decreasing.
4	Share capital	Increases because the company issues fresh capital to the public for listing.	Number of shares increases in dilutive FPO and remains the same in non-dilutive FPO
5	Cost for the Company	It is quite expensive	Compared to an IPO, the cost of an FPO is relatively low.
6	Risk factor	Investing in an IPO is more risky since there's usually not much information about the issuing company.	Information on the issuing company is readily available, which makes investing in an FPO relatively less risky.
7	Ownership dilution	Ownership gets diluted in an IPO.	Depending on the type of FPO, there may or may not be a dilution of ownership.

8	Purpose	The purpose of raising funds through IPO is to raise additional capital from the public.	The purpose of a company to diversify its equity base issues an FPO.
9	Types/Offers	Two types of shares in an IPO are equity and preference shares	FPO is also of two types, i.e. dilutive and non-dilutive.
10	Evaluation	Investors need to go through a company in detail while investing in an IPO. Since it is highly risky, only experienced and knowledgeable investors tend to invest in IPOs.	In FPOs, since investors know how a company performed after issuing its IPO, making an investment decision becomes more uncomplicated.

Thus, it has cleared that, No investment option is best for everyone. Each one has pros and cons. It depends on the risk level and goals. The investor risk levels need to be extremely high to invest in an IPO because they do not have much idea about the company, whereas, an FPO is relatively a safer bet for individual investors and new investors. Investing in an IPO requires more research than FPO. So here is need to understand the company fundamentals for long term investment, with a good risk appetite and have faith in the company.

1.3. (B) Secondary Capital Market (Stock Exchange)

The secondary market is a pre-requisite market for developing a capital market. This market facilitates marketability and liquidity of the corporate securities. Without this market, the corporate sector cannot grow. It is the economic barometer of the country. It indicates the economic growth of the nation. It facilitates the flow of capital into profitable enterprises. It has a significant impact on the business activities of the country. The trading activity takes place between investor through the intermediaries called stock brokers. Stock brokers assist the investors in buying and selling of securities in the secondary market. They buy or sell securities for their clients. Usually the secondary market transactions are completed through the stock exchanges. The secondary market for a variety of assets can vary from loans to stocks, from fragmented to centralized and from illiquid to very liquid.

(B).1 Meaning:

The secondary market is a market for existing financial securities. After the securities are originally sold through the primary market, they are traded through the secondary market. Thus the secondary market involves the purchases and sale of securities already issued. It is also called stock market or the aftermarket, is the financial market in which previously issued financial instruments such as stock, bonds, options and futures are bought and sold. A stock exchange is a market where shares and debentures of joint stock companies and securities of central, state and semi-Government bodies are bought and sold under a code of rules and regulation.

The Securities Contracts (Regulations) Act 1956 defines Stock Exchange *"as an association, organization or body of individuals whether incorporated or not, established for the purpose of assisting, regulating and controlling business in buying and selling and dealing in securities"*.

The said definition clearly indicates that a stock exchange is a capital market where long term finance for the development of companies can be obtained by selling the securities through authorized persons. The securities of government, quasi-government and private enterprises are bought and sold in this market. It is the nerve centre of national finance. Stock Exchange is, in fact the focal points of the capital market system that fuel the growth and expansion of national business, to the ultimate benefit and well-being of the national economy and its people.

Characteristics:

1. It is an organized market for the securities.
2. It may be an incorporated company or an association of person.
3. It regulates and controls business in buying, selling and dealing in securities.
4. The working of stock exchange is regulated by the Government.
5. Stock exchange does not itself engage in the purchase and sale of securities. It provides only a place where members can carry on their business on their own account under a code of rules and regulations.

The significance of stock exchange is found in its operation of smooth marketability and liquidity of corporate securities. It provides ready market for buying and selling of corporate securities. This market creates a favourable demand for stock and shares and with this demand company can improve their performance. It also creates an image for a company. It facilitates the self assessment of financial status of the corporate enterprise. It provides capital formation and promotes industrial growth of the country by attracting investment from the general public. This is an organized market for buying and selling of securities. The securities are evaluated through the floated price on every day operation. The listed securities gain quick response from the public in the market. Due to variation in price every day, the corporate enterprises can improve their bargaining position. There is no uniformity in the form or ownership of stock exchanges that are functioning in the country today. Some Stock exchanges are organized as voluntary associations and some are limited companies and some are guaranteed companies

(B). 2 Role and Functions of Stock Exchange:

The major role and important functions of stock exchange are as under:

1. ***Ready and continuous Market:*** Stock exchange provides a market place for exchange of securities freely by the brokers for their clients. It provides a ready and continuous market for buying and selling of securities i.e., shares, debentures and securities of Government and semi-Government bodies. Mobility of capital takes place smoothly.

2. ***Provides liquidity to investors:*** A continuous market facilitates liquidity through sale and purchase of securities. Any time, securities can be converted into cash and vice-versa. The liquidity increases the value and use of securities.

3. ***Wide distribution of securities:*** Stock exchange helps existing and new companies in wider distribution of their securities. Listed shares in the stock exchange are more acceptable and fetch higher market value. Listed securities are attracting investors from different parts of the country.

4. ***Mobilization of savings:*** The stock markets are perfect market which helps to mobilize the savings of the people to productive channels. They encourage individuals and institutions to invest their funds in business enterprises. It has facilitated the conversion of small savings of the public into productive activities. Thus there will be orderly flow of savings into investment and assist economic prosperity.

5. ***Ensure safety of funds:*** Stock exchanges ensure safety of investable funds because they have to operate under a code of rules and regulations. The brokers cannot overcharge the investors. This strengthens investors' confidence and stimulates large investments.

6. ***Proper direction to the flow of capital:*** Stock exchanges bring about flow of capital in appropriate directions; they direct the flow of capital in the most profitable channels. The prices quoted for different securities on the stock exchange indicate their relative profitability. If the securities are quoted in the stock exchanges above par for a long time, it indicates the good prospects of the concern. It is treated as a barometer of business activity.

7. ***Assessment of securities:*** The stock exchange ensures correct appraisal of security. The real worth of securities is evaluated by free play at market force. The prices quoted in the stock exchanges for all securities are recorded and made available to the public. This helps the investor to know the prices and value of securities at any time. The free play of demand for the supply of securities determines price continuously.

8. ***Mirror of business cycle /Economic Barometer:*** Stock exchanges are the mirror of business cycle. Price trends on a stock exchange reflect the economic progress and socio-political conditions of a country. It indicates the boom or depression prevailing in the country**.** Like barometer which indicates the variation in temperature of the environment at any point of time, the stock exchange indicates the health of the economy.

9. ***Capital Formation:*** Stock exchange play a vital role to form the capital required by corporate enterprises. Besides motivating public to invest in securities, the stock market promotes capital formation and provides necessary funds to the needy industries. Capital formation and disbursement is an auto mechanism found in stock exchange.

10. ***Help to banks:*** The Stock exchanges help banks to maintain liquidity by increasing the volume of marketable securities. They have mutual cooperation between banks and stock exchange. This facilitates speedy economic development and fair dealing in buying and selling securities

11. ***Future Forecast:*** Stock exchanges render forecasting function. The price movements for securities reflect and forecast the future happenings in business

operations. The impending business boom or depression is indicated in advance by stock exchanges. Prompt signal is given by the stock exchange in this direction.

12. ***Speculation:*** The operators on the stock exchange are the authorized agents with different names. These operators hold corporate securities for a temporary period. The speculators, who wish to make profit out of variation in price of securities, operate skillfully and provide good liquidity position to the securities. Speculation affects the share prices badly at certain time; it plays a vital role in moving the capital market.

(B).3 Online Trading Procedure on a Stock Exchange

Before starting the selling of company's securities through the stock exchange, firstly they have to get their securities listed on the stock exchange and the authorities of the stock exchange are satisfied with the financial soundness of the company. Earlier, the buying and selling of securities were done on the trading floor of the stock exchange. However, at present, it is done through online trading procedure. Basically there are four steps of online trading procedure in India i.e., (1) Find a stockbroker, (2) Open demat and trading account, (3) Login to demat and trading account and add money (4) View stock details and start trading. Actually for detail information there are following steps of online trading procedure:

1. **Selection of Broker:** The first step of the online trading procedure is the selection of a broker who will buy or sell securities on the behalf of investor. Broker may be an individual, partnership firm or corporate body but it is a member of stock exchange. Before placing an order to the registered broker, the investor has to provide necessary information, like, PAN Number, Birth date and Address, Occupation, Residential Status, Bank and Depository A/c details. After getting information regarding all the said things, the broker is ready to opens an online trading account in the name of the investor.

2. **Opening Demat Account with Depository:** The second step of the trading procedure is the opening of a Demat (Dematerialized) Account. A depository is an organization, which holds securities in electronic form like bonds, shares, debentures, etc. (At present NSDL and CDSL are two depositories). The depository and the investor do not have direct contact with each other. They interact with each other through depository participants only. The depository

participant will have to maintain the securities account balances of the investor and intimate investor from time to time about the status of their holdings.

3. **Placing the Order:** After the opening of a Demat Account, the next step is to placing of an order by the investor. The investor can place the order to the broker either personally or through email or phone. The investor must make sure that the order placed clearly specifies the range or price at which the securities can be sold or bought. For eg. an order placed by Mr. Ajay is Buy 100 equity shares of Infosys for no more than at 200 per share.

4. **Match the Share and Best Price:** The broker after receiving an order from the investor, it will have to then go online and connect to the main stock exchange to match the share and best price available.

5. **Executing Order:** The next steps, when the shares can be bought or sold at the price mentioned by the investor, it will be communicated to the broker terminal, and then the order will be executed electronically. Once the order has been executed, the broker will issue a trade confirmation slip to the investors.

6. **Issue of Contract Note:** Once the trade has been executed within 24 hours, the broker will issue a contract note. It is an essential legal document and helps in settling disputes claims between the investors and the brokers. A contract note as a printed unique order code number assigned to each transaction by the Stock Exchange. It consists of the details of shares bought or sold, the date, time; price of securities deal and brokerage charges.

7. **Delivery of Share and making Payment:** In the next step, the investor has to deliver the shares sold or to make payment for the shares bought. The investor has to do so immediately after receiving the contract note or before the day when the broker shall make delivery of shares to the exchange or make payment. This is known as pay in day.

8. **Settlement Cycle: Online or cash** payment of securities or delivery of securities is done on Pay in Day, which is within two days from transaction. It is because with effect from 2003 the settlement cycle is within two days from transaction. For Eg., if the transaction took place on Monday, then the payment must be done before Wednesday.

9. **Shares Delivery or Making Payment:** Within two days from the transaction, the Stock Exchange will then deliver the share or make payment to the other broker. This is known as pay out day. Once the shares have been delivered of payment has been made, the broker has to make payment to the investor within 24 hours of the pay-out day, as he/she has already received payment from the exchange.

10. **Delivery of Shares in Demat Form:** The last step of the trading procedure is making delivery or shares in Demat form by the broker directly to the Demat Account of the investor. The investor is obligated to give details of his Demat Account and instruct his Depository Participant for taking delivery of securities directly in his beneficial owner account.

Practical work:

1. *Secondary Capital Market (Stock Exchange) is an "Economic Barometer" of the nation. Explain its performance with practical aspects.*
2. *Visit the website of any stock market and analyzed its functions.*
3. *Briefly, draft the online trading procedure of stock exchange.*

(B). 4 Role of SEBI in regulating Capital Market in India

With the growth in the dealings of stock markets, lot of malpractices also started in stock markets such as price rigging, unauthorized premium on new issue and delay in delivery of shares, violation of rules and regulations of stock exchange and listing requirements. Due to these malpractices the customers started losing confidence and faith in the stock exchange. So government of India decided to set up regulatory body known as SEBI. It promotes orderly and healthy development in the stock market but initially SEBI was not able to exercise complete control over the stock market transactions. It was left as a watch dog to observe the activities but was found ineffective in regulating and controlling them. As a result in May 1992, SEBI was granted legal status. SEBI is a body corporate having a separate legal existence and perpetual succession.

It is the regulator for the securities market in India. Initially SEBI was a non statutory body without any statutory power. In April 1988 the SEBI was constituted as the regulator of capital markets in India under a resolution of the Government of

India. It became an autonomous body by the Government of India on 12 April 1992 and given additional statutory powers in the Securities and Exchange Board of India Act, 1992 being passed by the Indian Parliament. SEBI has its headquarters at the business district of Bandra Kurla Complex in Mumbai and has Northern, Eastern, Southern and Western Regional Offices in New Delhi, Kolkata, Chennai and Ahmedabad respectively. Controller of Capital Issues was the regulatory authority before SEBI came into existence; it derived authority from the Capital Issues (Control) Act, 1947.

The Preamble of the SEBI describes the basic functions of the Securities and Exchange Board of India as "*...to protect the interests of investors in securities and to promote the development of, and to regulate the securities market and for matters connected there with or incidental there to".* The main purpose of SEBI is to check on malpractices and protect the interest of investors. Hence, SEBI has to be responsive to meet the needs of three groups, such as: (1) Issuers, (2) Investors and (3) Intermediaries

SEBI has performed three functions rolled into one body: quasi-legislative, quasi-judicial and quasi-executive. It drafts regulations in its legislative capacity, it conducts investigation and enforcement action in its executive function and it passes rulings and orders in its judicial capacity. SEBI has taken a very proactive role in streamlining disclosure requirements to international standards. The main objectives of SEBI are:

a. To protect investors to have continuous flow of saving in stock market.

b. To try to make companies to use proper customes and to help them in selling securities at minimum expenses.

c. To help in obtaining efficient services to investors from market agent, bankers and other middlemen.

Role of SEBI:

The overall objectives of SEBI are to protect the interest of investors and to promote the development of stock exchange and to regulate the activities of stock market. In this context the SEBI performs the important three functional role to meet its objectives, which is given below:

1. **Role of Protective Functions:**

These functions are performed by SEBI to protect the trust and interest of investor and provide safety of investment. It includes the following sub-functions**:**

(a) ***It Checks Price Rigging:*** Price rigging refers to manipulating the prices of securities with the main objective of inflating or depressing the market price of securities. SEBI prohibits such practice regularly because this can defraud and cheat the investors.

(b) ***It Prohibits Insider trading:*** SEBI keeps a strict verify when insiders are buying securities of the company and takes action on insider trading. Insider is any person connected with the company such as directors, promoters etc. These insiders have sensitive information which affects the prices of securities.

(c) ***Prohibits fake and Unfair Trade Practices:*** SEBI does not allow to any companies to make misleading statements which are likely to induce the sale or purchase of securities by any other person.

(d) ***Orientation to Investors:*** SEBI undertakes steps to educate investors so that they are able to evaluate the various securities of different companies and select the most profitable securities.

(e) ***Apply Code of Conduct in Market:*** SEBI used to apply code of conduct in security market for promotion of fair practices with various steps such as: (i) It has issued informative guidance to protect the debenture-holders interest. (ii) It is empowered to investigate cases of insider trading and has provisions for stiff fine and imprisonment. (iii) It has stopped the practice of making preferential allotment of shares unrelated to market prices.

2. **Role of Developmental Functions:**

SEBI performed these functions to promote and develop activities in stock exchange and boost the business in stock exchange. Under developmental categories following functions are performed by SEBI:

(a) It promotes education and training to intermediaries of the securities market.

(b) It tries to support various activities of stock exchange for creating flexible and adoptable approach in following way: (i) It has permitted internet trading through registered stock brokers. (ii) It has made underwriting optional to reduce the cost of issue and (iii) Even initial public offer of primary market is permitted through stock exchange.

3. **Role of Regulatory Functions:**

These regulatory functions are performed by SEBI to regulate the business activities in stock exchange. To regulate the stock exchange following functions are performed:

(a) SEBI has framed various rules and regulations and code of conduct to regulate the intermediaries such as brokers, underwriters, merchant bankers, etc.

(b) These intermediaries have been brought under the regulatory purview and private placement has been made more restrictive.

(c) It has registers and regulates the working of stock brokers, sub-brokers, share transfer agents, trustees, merchant bankers and all those who are associated with stock exchange in any manner.

(d) SEBI regulates takeover of the companies and conducts inquiries and audit of stock exchanges.

(e) SEBI registers and regulates the working of mutual funds etc.

Thus with the help of different committees, SEBI has enjoyed success as a regulator by pushing systematic reforms aggressively and successively. SEBI is credited for quick movement towards making the markets electronic and paperless. SEBI has been active in setting up the regulations as required under law. SEBI has also been instrumental in taking quick and effective steps in light of the global meltdown.

Practical work:

1. *Prepare organization structure of Securities and Exchanges Board of India (SEBI)*
2. *Search and write the 'pros and cons' of SEBI*

1. 3. (C). Credit Rating and Depository Services

Credit Rating: It serves as a valuable input in the decision making process of different participants in the capital market including the regulators. Although credit rating is relatively new in India, the levels of awareness as well as its actual use are increasing slowly and gradually. With the liberalization and consequent restructuring of the financial services sector, credit rating is becoming even more important. Credit rating system have occupy an essential role as information providers particularly for credit related opinions in respect of debt instruments, a role that has been strengthened by the perception that their opinions are independent, objective, well researched and credible. Owing to this, it is an important that the major player in the market, particularly the investors, understand the significance and different agencies of credit rating.

(C). 1 Meaning: Credit Rating

Ratings, usually expressed in alphabetical or alphanumeric symbols, are a simple and easy understand tool enable the investor to differentiate between debt instruments on the basis of their underlying credit quality. The credit rating is a symbolic indicator of the current opinion of the relative capability of the issuer to service its debt obligation in a timely fashion, with specific reference to the instrument being rated. It is focused on communicating to the investors, the relative ranking of the default loss probability for a given fixed income investment in comparison with other rated instruments.

According to the–Standard & Poor's *"In determining a rating both quantitative and qualitative analysis are employed. The judgement is qualitative in nature and the role of the quantitative analysis is to help make the best possible overall qualitative judgement because, ultimately, a rating is an opinion"*

A rating is specific to a debt instrument and is intended as a grade, an analysis of the credit risk associated with the particular instrument. It is based upon the relative capability and willingness of the issuer of the instrument to service the debt obligations (both principal and interest) as per the terms of the contract. Thus, a rating is neither a general purpose evaluation on the issuer, nor an overall assessment of the credit risk likely to be involved in all the debts contracted or to be contracted by such entity. The primary objective of rating is to provide guidance to investor/ creditors in determining a credit risk associated with a debt instrument/ credit obligation. It does not amount to a recommendation to buy, hold or sell an instrument as it does not take into consideration factors such as market prices, personal risk preferences and other consideration which may influence an investment decision. The rating process is itself based on certain 'givens' the agency for instance does not perform an audit. Instead, it is required to rely on information provided by the issuer and collected by analysts from different source, including interactions in person with various entities. Consequently, the agency does not guarantee the completeness or accuracy of the information on which the rating is based.

(C). 1.1 Need of Credit Rating:

Credit rating plays vital role in financial market by helping to reduce the information asymmetric between lenders and investors. It provides ancillary business services and other services like risk management and consulting services to help financial institutions to manage credit and operational risks. The need and benefits of credit rating towards investors, borrowers, companies and government which reveals the following points

1. It enables the investor to identify the risks associated with various debt obligations.
2. It enables the investors to get superior information at low cast and help to take calculated risk in their investment decisions
3. It facilitates companies with good rating to enter the capital market confidently and raise funds at comparatively cheaper rates
4. It can be used as a marketing tool and encourage discipline among the corporate borrowers
5. It encourages people to invest their savings in corporate securities & get high return
6. It facilitates the formulation of public policy guidelines on institutional investments
7. Fair and good ratings motivate the public to invest their savings in good shares deposits and debentures.
8. Decreasing the potential conflict between the underwriters and the investors.
9. Providing greater liquidity in secondary market
10. Continuing growth of information technology, leads to encouraging increased disclosure on the part of companies.

11. Better accounting standards and improved financial information for the promotion of individual and institutional investor protection.
12. Increased securitization of borrowing and lending consequent to disintermediation
13. Increasing role of capital and money markets consequent to disintermediation
14. Globalization of the credit market and facilitates foreign collaborations
15. The growth of confidence in the efficiency of the market mechanism
16. Withdrawal of Government safety nets and the trend towards privatization.
17. Assess the creditworthiness of issuers of securities, usually companies, non-profit organizations / government.
18. Ample opportunities to strengthen the capital market and building investors' confidence in the Indian financial system.

Thus, it is clear that, in India, there are many systemic constraints on the credit rating services, for e.g- low disclosure levels; poor audit quality and long time lags in the availability of data. There is also a need to educate the investor to have the right expectations. All this has led to ratings being reduced from being an evaluation tool to a mere certification tool, thereby at times defeating the very purpose of existence of rating agencies.

(C). 1.2 Credit Rating Agencies in India:

In the economic globalization, liberalization, industrialization, industrial development and Research promoted by disintermediation, there is a genuine need for authentic investment information designed to facilitate the decision making process of investors and other participants of the financial services sector. There are various credit rating agencies in India. Such as:

(a) Credit Rating Information Services of India Limited (CRISIL)-

CRISIL, the first rating agency in India, which was mainly promoted by the Industrial Credit and Investment Corporation of India (ICICI) and Unit Trust of India (UTI) in 1987. They have other shareholders, it includes Life Insurance Corporation of India (LIC), State Bank of India (SBI), Asian Development Bank (ADB), Housing Development Finance Corporation (HDFC), General Insurance Corporation of India

(GIC) and its subsidiaries, Standard Chartered Bank, Bank of Tokyo, Banque IndoSuez, Sakura Bank, Hong Kong and Shanghai Banking Corporation, Citibank, Grindlays Bank, Duetsche Bank, Societe Generale, Banque Nationale de Paris, UCO Bank, Bank of India, Canara Bank, Allahabad Bank, Central Bank of India, Vysya Bank Ltd, Bank of Madura Ltd, & Indian Overseas Bank.

The principal objective of CRISIL is to rate debt obligations of Indian companies. It provides rating guide to the investors as to the degree of certainty with timely payment of interest and principal on a particular debt instruments. CRISIL, rates debentures, fixed deposit programs, short term instruments like commercial paper, structured obligations and preference shares. CRISIL has rated in all 926 debt instruments issued by 668 companies from its commencement in 31st March1994. They have introduced CRISIL Card, CRISIL View, CRISIL Ban card and CRISIL Rating Digest Service.

(b) Investment Information & Credit Rating Agency of India Limited (ICRA)

The IFCI and a number of other financial institutions established ICRA in 1991 at Delhi. It undertakes rating of debt instruments. ICRA credit rating provides an investor with a simple indicator expressing the underlying credit quality in a debt issue programme. ICRA credit ratings also establish a connection between risk and return.

They provide a yardstick against which to measure the risk inborn in an instrument. An investor uses the rating to assess the risk level and compares the offered rate of return with his expected rate of return (for the given level of risk) to optimize his risk-return trade off. The relatively unknown issuer is also benefited by having access to a much wider investor base as credit rating minimizes the role of ‘name recognition’ in an investment decision. In addition, ICRA provides ‘general assessment’ report on different aspects of the company’s operations and management.

(c) Credit Analysis and Research Limited (CARE)

The Industrial Development Bank of India (IDBI) jointly with Canara Bank, UTI, private sector banks and financial services companies promoted the Credit Analysis and Research Institution to offer credit rating information and equity research service to the Indian industry and business institutions. CARE, incorporated on April 21, 1993, commenced its operations in October 1993.

CARE undertakes rating of all types of debt instruments like commercial paper, fixed deposits, bonds, debentures and structural obligations, involving an independent and professional assessment of debt servicing capabilities of companies. Business organization gets necessary information and guidance on equity research services and credit rating system.

(d) Duff and Phelps Credit Rating India Private Ltd. (DCR)

This is the leading international credit rating agency. Duff and Phelps with the J.M. Financial and Alliance Group set up DCR in India. It has started rating the company's debt instruments since 1996. It has provided effective competition to the existing agencies. The main objective of DCR is to give credit rating to debt instruments. Various agencies are expected to publicize the ratings and also update the rating on a quarterly basis.

The guidelines given by SEBI for rating function and brought them under its regulatory framework. CRAs are required to attain a minimum net worth of Rs.5 crores. They are prohibited from rating the instruments floated by their promoters and also borrowers of promoters' institutions. There are popular symbol employed by this agency such as: D1, D_2, D_3 etc., It is depending upon the credit status.

(e) Onida Individual Credit Rating Agency Ltd. (ONICRA)

This credit rating agency has been setup and sponsored by the Onida Finance Ltd. It is known as 'ONICRA'. It has taken up the task of credit rating individual borrowers and not an institutional borrower. Hence, ONICRA helps the users of this rating to know risk level associated with entering into the credit transactions. It is gradually gaining acceptance among financial institutions and others. Brickwork / stonework ratings are the newest rating agencies in the country.

(f) Fitch Ratings (India) Ltd.

Fitch Ratings Limited is also one of the good rating agency in India, which is a 100% owned subsidiary of a foreign company. It is recognized by the Securities Exchange Board of India (SEBI), for its operations in India. This rating agency provides necessary guidance to investor for the determining a credit risk associated with a debt instrument.

(C). 1.3 Credit Rating Methodology:

An evaluation and monitoring ratings, both qualitative and quantitative criteria are employed. The methodology involves an analysis on various sections of the past performance of the company and an assessment of its future prospects, which involves judgment of the company's competitive advantage position and assessment of its management and strategies. In order to reduce subjectivity, a meaningful decision-making process is applied in assigning a rating which ensures that no single individual decides on a rating.

The operation of rating exercise commences at the request of a company. A rating applies to a particular debt obligation of the company and is not a general purpose evaluation of the company. The focus of the assessment is on the ability and the willingness of the company to meet the financial obligations on the debt instrument in a timely manner. The following key factors should consider in the credit rating methodology:

Business Analysis- It includes risk of industry, market position of the company within the industry, operating efficiency of the company and administrative cum legal position.

Financial Analysis- It covers quality of accounting with its procedure, earning protection, trend of cash flow and adequacy of financial flexibility etc.

Management Evaluation- It focuses the track record of the management, mission and goal of company, depth of managerial talent, succession plans, capacity appraisal to overcome adverse situations, philosophy and its managerial strategies.

Regulatory and Competitive Environment- This part deals with structure and regulatory framework of the financial system, trends in regulation or deregulation and their impact on the company.

Fundamental Evaluation- It includes capital adequacy, assets quality, liquidity management, profitability ratio and financial position, Interest & tax sensitivity etc.

Thus, the credit ratings are the symbolic presentation of opinions' of concern agency. The various symbols are used by above different agency. The classification of ratings is on the basis of merits. It has mainly four categories, such as: (1) High investment grade, (2) Investment grade, (3) Speculative grade (4) Poor grade

Practical work:

1. How the Credit rating service as a 'valuable inputs' in decision making process of different participants in the capital market? Justify.

2. Understand and fill the following table of four Indian Credit Rating Agencies.

3. Discuss and write the credit rating methodology by considering the key factors.

Agencies' Name	Established year	Established place	Objectives	Functions	Present performance
CRISIL					
ICRA					
DCR					
ONICRA					

(C). 2 Depository Services

A depository institution provides financial services to personal and business customers. Deposits in the institution include securities such as stocks or bonds. The institution holds the securities in electronic form also known as book-entry form, or in dematerialized or paper format such as a physical certificate. The rapid growth in numbers, volumes and value of securities exposed the limitation of handling and dealing in securities in physical mode. The trading in physical segment is full of inefficiencies due to handling of large volumes of certificates and also involves various other problems like bad deliveries, delays in transfer, irregular settlement, loss in transit, forgery certificates, stolen certificates, mutilation of certificates, postal losses, court cases, litigation etc. To overcome these deficiencies, a new system of trading, viz. Depository system was introduced, which facilitates investor to hold securities in electronic form and to trade in these securities. The depository bought in solutions for all these problems.

Technology is revolutionizing every field of human effort and activity, especially in the capital markets. A major development has been the setting up of depository services. The objective of a depository is to provide for the maintenance or transfer of ownership records of securities in an electronic form and scripless trading in the stock exchanges, thereby reducing settlement risks. The Securities and Exchange Board of India (SEBI) has granted registration to two depositories - e National Securities Depository Limited (NSDL) and the Central Depository Services (India) Limited (CDSL) under the Depository Act, 1996. This provided the capital markets with superior technology, complex securities processing and rock solid accounting and portfolio management system.

(C). 2.1 Meaning: Depository

A depository in a simple term means a place where something is deposit for storage and security, however in capital market, this term has a lot of relevance, we define ***"Depository as an institution that works like bank"*** Likewise our bank holds investor fund, similarly depository maintains an account for investors securities (share, debentures, mutual fund etc) hold by them in a dematerialized or an electronic form.

Depository is an organization which holds your securities in electronic (known as 'book entry') form, in the same manner as a bank holds your money. Further, a depository also transfers your securities without actually handling securities, in the same day as a bank transfers funds without actually handling cash. In simple terms Depository is an institution or organization which holds securities with it, in which trading is done among shares, debentures, mutual funds, derivatives and commodities. The intermediaries perform their actions in variety of securities at Depository on behalf of their clients. These intermediaries are known as Depositories Participants.

A depository can be compared to a bank. A depository is an organization where the securities of an investor are hold in electronic form and carries out the securities transaction by book entry. It means, just as a bank holds cash in your account and provides all services related to transaction of cash, a depository holds securities in electronic form and provides all services related to transaction of shares/debt instruments. A depository interfaces with its investors through its agents called Depository Participants (DPs). If an investor wants to utilize the services offered by a depository, the investor has to open an account with a DP. This is similar to opening an account with any branch of a bank in order to utilize the bank's services. Thus, an investor who wishes to avail of all depository services has to open a demat account with a depository participant. The depository participant is an agent of the depository and is authorized to offer depository services to investors. According to SEBI guidelines, financial institutions, banks, custodians, stock brokers can become depository participants. Once you have opened an account with a depository participant, you can buy or sell shares in the electronic form, provided the seller/buyer also holds shares in the electronic form.

Features of Depository System:

(a) Day-to-day basis of reconciliation is made by NSDL

(b) Securities are divisible and, as such, can be transacted by any quantity;

(c) Allotted securities as International Security Identification Number (ISIN) by SEBI

(d) The benefit of depository system is enjoyed by the investor of securities

(e) CDSL and NSDL are the Depository Participants to act as agent.

Transferring the ownership of shares from one investor's account to another investor's account when a trade is executed is one of the primary functions of a depository. This helps reduce the paperwork for executing a trade and speeds up the transfer process. Moreover a depository is it eliminates the risk of holding the securities in physical form such as theft, loss, fraud, damage or delay in deliveries. Depository services include checking and savings accounts and the transfer of funds and electronic payments through online banking or debit cards. The Depository has various depository participants registered with it which offer depository services or Demat account services to their clients.

Who are the depositories? Depositories are those who are licensed by the SEBI to undertake depository functions i.e. holding and handling of securities in electronic form. The NSDL promoted by UTI, IDBI and NSE is the first depository of India. The Stock Exchange, Mumbai has promoted CDSL which has drawn plans to set up the second depository in the country

Process of Depository: There are three steps in which an investor can covert his physical certificate into electronic form.

1. Open an account with one of the Depository Participants of NSDL

2. Sign an Agreement with the Depository Participants

3. Submit dematerialization request form along with share certificate to issuer.

Dematerialization (Demat) Account and its Process: It is an account that holds the investors securities such as shares, debentures, mutual fund etc in a dematerialized or an electronic form. A buy transaction will result in a credit entry while a sell transaction leads to debit entry in a demat account. A demat account is opened on the same lines as that of a Bank Account. Prescribed Account opening forms are available with the Depository Participants, needs to be filled in. Standard Agreements are to be signed by the Client and the Depository Participants, which details the rights and obligations of both parties. Along with the form the client requires to attach photographs of account holder, attested copies of proof of residence and proof of identity needs to be submitted along with the account opening form. If the corporate clients, need of additional attachments are - true copy of the resolution for Demat account opening with signatories to operate the account and true copy of the Memorandum and Articles of Association is to be attached.

After the opening as account, all existing shares can be dematerialized and converted into Electronic Form. Dematerialization is a process by which investor can deposit (demat) shares of any company listed on NSDL which are registered in investor name and convert the physical holdings into electronic form as under:

a. Fill a Dematerialization request form available with participant.

b. Submit share certificates along with request form.

c. Investor account will be credited within 15 days.

d. If investor wishes to convert their electronic shares back to physical shares at a later stage, they do so by applying for re-materialization, submit it for dematerialization

C). 2.2 Benefits of Depository System

A depository eliminates the risk associated with holding physical securities. They reduce the paper work involved in trading and faster the transfer of shares. In 1996, demat or electronic trading was made compulsory for institutional investors, which led to a spike in the overall trading volumes in the Indian market. Foreign investors felt more confident about trading in the Indian market due to the depository system as there were far fewer incidents of forgery, delay and unscrupulous transfer of shares. The benefits of depository system may be studied under four heads namely:

I. Benefits to investors

a. It eliminates bad deliveries

b. It computes the settlement cycle very fast

c. It makes quick transfer and registration of securities and help investor to get dividend and bonus without delay.

d. It eliminates all risks associated with physical certificate

e. It makes to provides nomination facility to the investors

f. It helps to reduces trading cost and exempt from stamp duty on transaction.

g. Being it is paperless trading; no share certificate and deed etc. are required.

h. It charge interest rate on loan against pledge of dematerialized shares is comparatively lower.

i. Use the account holder can totally freeze his account for any desired period.

j. It enables the investors to deliver shares in any part of the country without exposing themselves to the risk and cost of transportation.

k. It enables to revise the investors' portfolio more frequently due to low transaction costs and quick transfer of securities.

II. Benefits to Capital Market

1. Dues are settled in a very short time
2. It also eliminates bad delivering
3. It quick solved the problems arising from odd lots of securities
4. It eliminates the physical handling of documents and encourage paperless work
5. It is more transparent, efficient and reduces errors
6. Questions of loss, damage of securities does not arise.
7. Huge number of transactions can be settled at a very short time.
8. Build high degree confidence of investors in the capital market.

9. Use of depository system attracts foreign investors.
10. Volume of trade in capital market substantially increases.
11. Increased in participation of middle income class directly/through mutual funds

III. Benefits to Company

a. It reduces the risk of loss of securities and eradicate the fake activities;
b. It avoids the checking of shares, deeds and various papers
c. No share certificate is issued as the securities are divisible
d. It reduces the various costs which require secretarial help
e. Scriptless trading helps allocate corporate benefits faster.
f. It supplies better communication facilities
g. It helps the shareholder to take decisions through quick availability of information
h. It enables the company to maintain and update stock information.
i. Issue cost gets drastically reduced due to dematerialization of securities.
j. Paperless trading is a boon for the company management.
k. It helps the company build a good corporate image.

IV. Benefits to Intermediaries:

1. It helps to enhanced liquidity, safety and turnover on stock market.
2. It improved cash flow elimination of forgery and counterfeit
3. Elimination of risk from settlement due to bad deliveries.
4. No postal / courier charges
5. Periodic status reports to investors on their transactions, leads to better controls

(C). 2.3 Present Position and Forms of Depository in India

In India long back when at the Bombay Stock Exchange, stocks were traded in rings and when deals were fixed money was exchanged for receipts. Later physical shares certificates were provided. This invited a lot manual paper work and physical process also led to scams. Investor used to hold the securities in the form of physical certificate which has their own disadvantages and to take a control over the irregularities of the capital market for the protection of an investor`s interest. It means the rapid growth in numbers; volumes and value of securities exposed the limitation of handling and dealing in securities in physical mode. The trading in physical segment is full of inefficiencies due to handling of large volumes of certificates and also involves various problems. Depository system has been introduced in India where the securities could be handled in an electronic form by the process of dematerialization. After introduced the Dematerialization in 1996, that entire process was digitized and shares were transferred electronically in "Demat Account". This depository bought in solutions for all these problems. A major development has been the setting up of depository services. The objective of a depository is to provide for the maintenance or transfer of ownership records of securities in an electronic form and scripless trading in the stock exchanges, thereby reducing settlement risks. The Securities and Exchange Board of India (SEBI) has granted registration for two depositories in India which are well known as NSDL (National securities depository limited) and CDSL (Central Depository Services (India) Limited) under the Depository Act, 1996. They interface with the investors through their agents called Depository participants (DPs). DPs could be the banks (private, public and foreign), financial institutions and SEBI registered trading members. There are mainly three parties involved in Depository System:

- *Depository:* facilitates the smooth flow of trading and ensure the investor`s about their investment in securities
- *Depository Participant (DP):* provides the service of opening a demat account to the investor.
- *Investor:* individual or group invested in securities

Depository participant provides the service of opening a demat account to the investor; they are coming with different schemes like three-in-one demat account, free demat account etc to attract the investors to open an account with them. However, they are making an investment in to securities more accessible by providing services like SMS, e-mail for every transaction, E-trading platform, investment advice etc.

In India, Depository Participant is described as an agent of the depository. They are the mediators between the depository and the investors. The relationship between the Depository Participants and the depository is governed by an agreement made between the two under the Depositories Act. In legal sense, a Depository Participant is an entity who is registered under the section 12 (1A) of the SEBI Act. As per the Act, a Depository Participant can offer depository-related services only after obtaining a certificate of registration from SEBI. As of 2012, there were 288 of NSDL and 563 of CDSL registered Depository Participants with SEBI. As per the SEBI Regulations 1996, prescribe a minimum net worth of Rs. 50 lakh for stockbrokers, agents and non-banking finance companies (NBFC), for granting them a certificate of registration to act as Depository Participants. If a stockbroker seeks to act as a Depository Participants in more than one depository, he should comply with the specified net worth criterion separately for each such depository.

Thus, in the depository system, share certificates belonging to the investors are dematerialized and their names are entered in the records of depositary as beneficial owners. Investors' names in the companies register are replaced by the name of depository as the registered owner of the securities. The beneficial owner continues to enjoy all the rights and benefits and be subject to all the liabilities in respect of the securities held by the depository. The ownership changes in, the depositary are done automatically on the basis of delivery vs. payment. The investors opting to join depository mode are required to enter into agreement with depository through a participant who acts as an agent of depository. The agencies such as custodians, bank, financial institutions, large corporate brokerage firms, non-banking financial companies etc. act as participants of depositaries. The companies issuing securities are also required to enter into an agreement with the depositary.

Form of Depository in India: A depository is an organization that holds securities of investors in an electronic format at the request of an investor through a registered Depository Participant. It assists in the allotment and transfer of securities and securities lending. In a depository, securities such as money, shares and properties, etc. are kept for safekeeping under their or depositary terms. The securities are held in the form of electronic accounts. They carry out their various operations through functionaries called as business partners or a Depository Participant. This system is governed under the Depositories Act by the government. The enactment of this act paved the way for the establishment of NSDL and CDSL. NSDL stands for 'National

Securities Depository Limited', whereas CDSL stands for 'Central Depository Services Limited'. They both are depositories that hold various securities like shares in electronic form. There is no major difference between the two; however there is small difference in their charges and their source of work. NSDL works for National Stock Exchange, whereas CDSL works for Bombay (Mumbai) Stock Exchange. Let us make an in-depth study of NSDL depository system as under:

(C). 2.3.1 National Securities Depository Limited (NSDL)

The first and largest depository set up in India is National Securities Depository Limited (NSDL). It is promoted by Industrial Development Bank of India (IDBI) - the largest development bank of India, Unit Trust of India (UTI) - the largest mutual fund in India and National Stock Exchange (NSE) - the largest stock exchange in India. Some of the prominent banks in the country have taken a stake in NSDL i.e. State Bank of India, HDFC Bank Limited, Deutsche Bank A.G, Axis Bank Limited, Citibank, Oriental Bank of Commerce, Union Bank of India, Dena Bank, Canara Bank etc. It has established in August 1996 and actual operation was commenced in October 1996. The Depositories Act has provided dematerialization route to book entry based transfer of securities and settlement of securities trade. In exercise of the rights conferred by the Depositories Act, NSDL framed its Bye laws and business rules with the approved by SEBI. While the Bye Laws define the scope of the functioning of NSDL and its business partners; the Business Rules outline the operational procedures to be followed by NSDL and its Business Partners.

NSDL depository has promoted by institutions of national importance responsible for economic development of the country. Since beginning a national infrastructure of international standards that handles most of the securities held and settled in dematerialized form in the Indian capital market. Although India had a vibrant capital market which is more than a century old, the paper-based settlement of trades caused substantial problems like bad delivery, delays in transfer, irregular settlement till recently. NSDL aims to ensure the safety and soundness of Indian capital market places by developing settlement solutions that increase efficiency, minimize risk and reduce costs. Using modern and flexible technology systems, NSDL works to support the investors and brokers in the capital market of the country. In the depository system, securities are held in depository accounts, which is more or less similar to holding funds in bank accounts. Transfer of ownership of securities is done through simple account transfers. This method does away with all the risks and hassles normally associated with paperwork. Consequently, the cost of transacting in a depository environment is considerably lower as compared to transacting in certificates. Hence at NSDL, play a central role in developing products and services that will continue to nurture the growing needs of the financial services industry. In view of the amendment SEBI (Depositories and Participants) Regulations, 2012, NSDL has adopted code of conduct and ethics for its directors and top managerial personnel. These ethical code of NSDL, aimed at improving the professional and ethical standards in the functioning of the company thereby creating better investor confidence in the integrity of the market. The entire integrated system (including the electronic links and the software at NSDL and each business partner's end) is called the ***"NEST"*** (National Electronic Settlement and Transfer) system.

NSDL has introduced a Certification Programme in Depository Operations, and it has been made compulsory for all Depository Participants to appoint a person qualified in this certification in each of its branches. All grievances of the investors are to be resolved by the concerned business partner. If they fail to do so, the investor has the right to approach NSDL. They has taken a comprehensive insurance policy to help Depository Participants to indemnifying investors for the loss accrued to them due to errors, omissions, commission or negligence of Depository Participants. NSDL and its business partners use computer technology systems, which conform to industry standards. Further, the systems are accepted by NSDL only after a rigorous testing procedure. The NSDL computer systems are continuously reviewed in order to make them more secure and adequate for the size of business. These reviews are a part of an ongoing exercise wherein security considerations are given as much importance as operational efficiency.

Facilities and Services offered by NSDL: The following facilities and services are offered by NSDL to their investors, through its agents (Depository Participants).

1. Holding the investors' securities in electronic form.
2. Dematerialization and re-materialization of securities (converting physical certificates to electronic form and vice versa)
3. Transfer of securities
4. Settlement of trades in e-form in the depository segment of stock exchanges

5. Pledging or hypothecation of dematerialized securities;
6. Electronic credit of public offerings and non-cash corporate actions such as rights, bonus etc.

NSDL Measures to Ensure Safety in Investor Holdings, Such as:

1. As per the criteria prescribed by SEBI for becoming a Depository Participant in the regulations A Depository Participant can be operational only after registration by SEBI, which is based on the recommendation from NSDL.
2. Depository Participants are allowed to make any debit and credit entry to an account only on the basis of valid instruction from the client or investors.
3. There is mandatory reconciliation system between Depository Participants and NSDL every day.
4. Records of all transactions are maintained by NSDL with the databases of business partners.
5. Periodical inspections / verification has made of various activities of both Depository Participant and agent by NSDL.
6. Every investor has a right to receive statement of accounts periodically from the Depository Participant.
7. NSDL forwards statement of account to investors randomly for counter check in every month
8. Though the depository holds the investor accounts on trust, however investor have right to transfer their holdings to an account held with another Depository Participant
9. The protection measures adopted by NSDL are more than in the regulations prescribed by SEBI.
10. The data interchange between NSDL and its business partners is protected by protection measures of international standards such as encryption hardware lock.

(C). 2.3.2 Central Depository Services Limited (CDSL)

Central Depository Services Limited (CDSL) was received SEBI approval in February,1999 and commenced operation in July 15, 1999. It is second Depository (NSDL being first) in India to hold shares and securities in dematerialized form and classified as capital market infrastructure company. CSDL is promoted by the Bombay Stock Exchange (Mumbai), in association with the State Bank of India (SBI), Bank of India, Bank of Baroda and HDFC Bank. The objective of CDSL was to providing ***convenient, dependable and secure*** depository services at affordable cost to all market participants. To promote use of electronic form of securities and to encourage investor for dematerialization of existing physical paper based shareholding, Depository Act, 1996 exempted all depository based electronic transfer of shares and securities from Stamp Duty, which was 0.25 percent of the value of the securities. It has an attempt to ensure the safety and soundness of Indian market places by developing settlement solutions that increase efficiency, minimize risk and reduce costs. The investor who is known as beneficial owner has to open a demat account through any Depository Participant for dematerialization of his holdings and transferring securities. The balances in the investors account recorded and maintained with CDSL can be obtained through the Depository Participant. The Depository Participant is required to provide the investor, at regular intervals, a statement of account which gives the details of the securities holdings and transactions. The depository system has effectively eliminated paper-based certificates which were level to be fake, forged, counterfeit resulting in bad deliveries. CDSL offers an efficient and instant transfer of securities.

Convenience: CDSL has a wide network of Depository Participants, operating from over 17,000 sites, across the country, offering convenience for an investor to select a Depository Participant based on his location. The Depository Participants are directly connected to CDSL thereby providing on-line and efficient depository service to investors. Wide Spectrum of Securities Available for Demat. The equity shares of almost all group companies are available for dematerialization on CDSL, consisting of Public (listed & unlisted) Limited and Private Limited companies. These securities include equities, bonds, units of mutual funds, Govt. securities, Commercial papers, Certificate of deposits; etc. Thus, an investor can hold almost all his securities in one account with CDSL. It has kept its tariffs very competitive to provide affordable depository services to investors.

Dependability: This system is built on centralized database architecture and thus enables Depository Participants to provide on-line depository services with the latest status of the investor's account. Convenient to Depository Participants the entire database of investors is stored centrally at CDSL. It has made provisions for contingency terminals, which enables a Depository Participants to update transactions, in case of any system related problems at the Depository Participants office. Continuous updation of procedures and processes in tune with evolving market practices is another hallmark of CDSL's services. CDSL conducts regular audit of its Depository Participants to ensure compliance of operational and regulatory requirements. CDSL has in place a mechanism for monitoring dormant accounts through helpdesk. Depository Participants and investors can obtain clarifications and guidance from CDSL's prompt and courteous helpline facility.

Security: All data held at CDSL is automatically mirrored at the Disaster Recovery site and is also backed up and stored in fireproof cabinets at the main and disaster recovery site. Every beneficial owner in CDSL is allotted a unique account number, which prevents any wrong entry or transfer of securities. If the transferor's account number is wrongly entered, the transaction will not go through the CDSL system, unless corrected. All data and communications between CDSL and its users is encrypted to ensure its security and integrity. In case any Depository Participants of CDSL goes into liquidation, the creditors of the Depository Participants will have no access to the holdings of the beneficial owner. CDSL has an insurance cover in the unlikely event of loss to a beneficial owner due to the negligence of CDSL or its Depository Participants.

Merits of NSDL and CDSL: In the depository system, the ownership and transfer of securities takes place by means of electronic book entries. This system rids the capital market of the dangers related to handling of paper. NSDL and CDSL provide numerous direct and indirect benefits, such as:

1. ***Eradication of bad deliveries* -** In the depository system holder of an investor are dematerialized, the question of bad delivery does not arise. In a depository environment good money certainly induce good quality of assets

2. ***Risk elimination in physical certificates*-** Dealing in physical securities have risks of theft, loss of certificates etc. This problem does not arise in the depository environment.

3. ***No stamp duty:*** For transfer of any kind of electronic securities in the depository. This waiver extends to equity shares, debt instruments and units of mutual funds.

4. ***Quick registration and transfer of securities-*** The ownership and transfer of securities takes place by means of electronic mode in the depository system. There is no further need to send it to the company's registrar for registration.

5. ***Faster settlement cycle-*** With the use of electronic record system, the settlement cycle of trading transaction is very fast without delay. It leads to faster turnover of stock and more liquidity with the investor.

6. ***Faster disbursement of non cash corporate benefits- like rights, bonus, etc. -*** NSDL provides for direct credit of non cash corporate benefits like rights, bonus etc., to an investors account, thereby ensuring faster disbursement and avoiding risk of loss of certificates in transit.

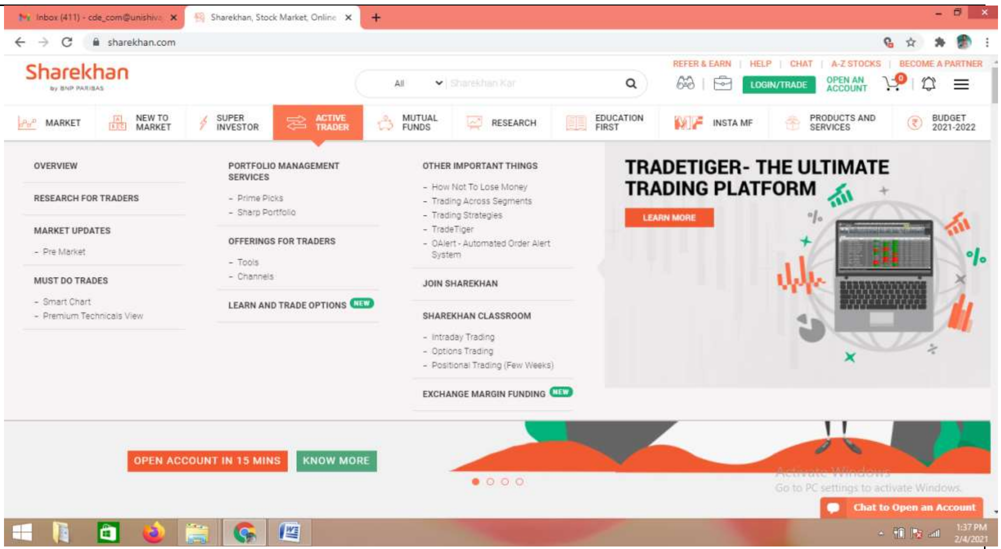
7. ***Periodic reports-*** Investors get periodical status report on their holdings and transactions. It leads to better controls.

8. ***Eradication of problems to transmission of demat shares-*** The process of transmission is more convenient in case of dematerialized holdings, as the transmission formalities for all securities held in a demat account.

9. ***Elimination of problems on selling securities of a minor -*** A natural guardian is not required to take court approval for selling demat securities on behalf of a minor.

- **Practical: Visit any Share broker office and observed share trading Activities:**

Practical No. 1: *Visit to Sharekhan trade broker office*



(https://www.sharekhan.com/, visited on dated 23December2020)

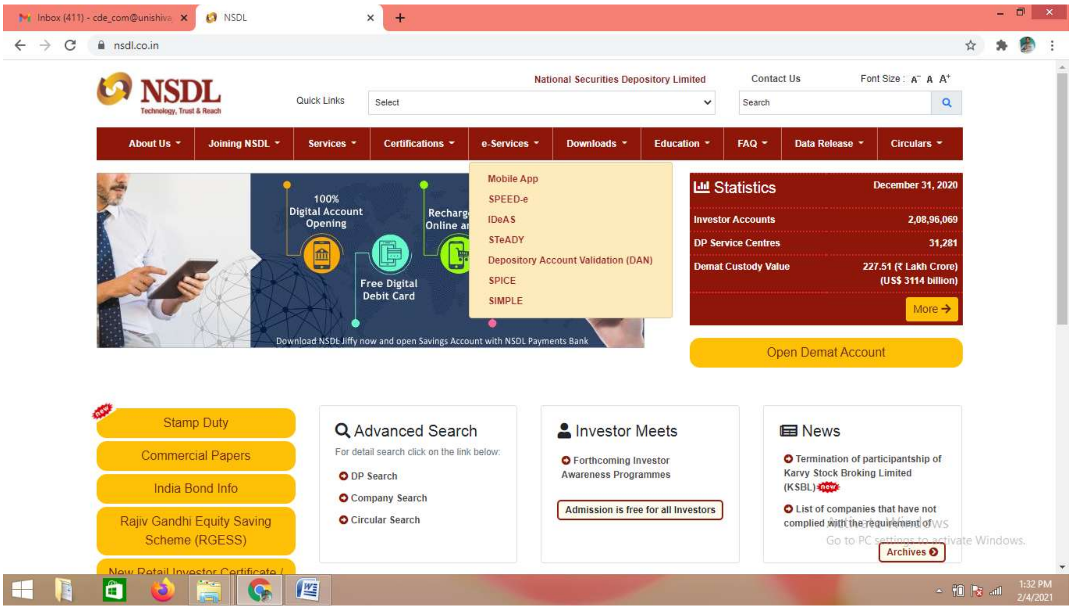
After the visit to sharekhan trade broker and mentioned following observations:

1. *It is seems that the Sharkan is one of the leading broker in share market.*
2. *It is noted that the Sharkhan provide portfolio management facilities to their clients.*
3. *It is observed that the Sharekhan serve facilities as equity share analysis and similar trading activities service, which helps to investor for investment decision making.*

In this way students should visit to any trading broking office e.g. ICICI, Mahindra Kotak, HDFC etc., nearby your location and mentioned your own observation.

Similarly, students should understand the how to open "Demat Account" by supporting necessary document and which helps to understand the procedure of Demat Account with the help of any stock broker / investment bank / merchant banker (e.g- Sherkhan)

Practical No. 2: Visit to website of depositories i.e., NSDL (National Securities Depository Limited) and CDSL (Central Depository Service Limited) and understand the process and role of depository system.



((Sources: https://www.nsdl.co.in/)

After visit to NSDL official website :

1. *It is observed that, the National Securities Depository Limited (NSDL) is a financial organization created to hold securities such as bonds, shares etc.*

2. *It is also seems that, basic facilities like account maintenance, dematerialisation, rematerialisation, settlement of trades through market transfers, off market transfers & inter-depository transfers, distribution of non-cash corporate actions and nomination/ transmission.*

In this way students should visit to Depositories website and point out other observation. Beside this students should Collect information on present position of Indian depository system both NSDL & CDSL and write highlights on same

1. 3. (D). Mutual Funds :

Financial sector is going through a phase where lots of new products, services are coming into the market. People, in general, feel that investment in stock market has a huge risk. In order to cope up with the requirement of diversification, liquidity and low risk; mutual fund evolved as an investment avenue. This facilitates lot of advantages to a small investor. Further, those who wish to invest their money and are able to share the profit can avail benefit of port-folio management where huge funds are given to fund managers who professionally manage the funds. On the other hand, there are people who do not have even access to basic banking services. It is important to bring them into mainstream for which financial inclusions drive is necessary. Micro finance is one of the way through which the needy people are provided financial services at affordable cost.

(D). 1 Concept: Mutual Funds

A mutual fund is a financial intermediary that pools the savings of investors for collective investment in a diversified portfolio of securities. A fund is "mutual" as all of its returns, minus its expenses, are shared by the fund's investors. The Securities and Exchange Board of India (Mutual Funds) Regulations, 1996 defines a mutual fund as a 'a fund established in the form of a trust to raise money through the sale of units to the public or a section of the public under one or more schemes for investing in securities, including money market instruments'. According to the above definition, a mutual fund in India can raise resources through sale of units to the public. It can be set up in the form of a Trust under the Indian Trust Act. The definition has been further extended by allowing mutual funds to diversify their activities in the following areas: Portfolio management services, Management of offshore funds, Providing advice to offshore funds, Management of pension or provident funds, Management of venture capital funds, Management of money market funds, Management of real estate funds.

A mutual fund serves as a link between the investor and the securities market by mobilising savings from the investors and investing them in the securities market to generate returns. Thus, a mutual fund is akin to portfolio management services (PMS). Although, both are conceptually same, they are different from each other. Portfolio management services are offered to high net worth individuals; taking into account their risk profile, their investments are managed separately. In the case of mutual funds, savings of small investors are pooled under a scheme and the returns are distributed in the same proportion in which the investments are made by the investors/unit-holders. Mutual fund is a collective savings scheme. Mutual funds play an important role in mobilising the savings of small investors and channelising the same for productive ventures in the Indian economy.

(D). 2 Importance of Mutual Funds

An investor can invest directly in individual securities or indirectly through a financial intermediary. Globally, mutual funds have established themselves as the means of investment for the retail investor.

1. Professional management: An average investor lacks the knowledge of capital market operations and does not have large resources to reap the benefits of investment. Hence, he requires the help of an expert. It, is not only expensive to 'hire the services' of an expert but it is more difficult to identify a real expert. Mutual funds are managed by professional managers who have the requisite skills and experience to analyze the performance and prospects of companies.

2. Portfolio diversification: An investor undertakes risk if he invests all his funds in a single scrip. Mutual funds invest in a number of companies across various industries and sectors. This diversification reduces the riskiness of the investments.

3. Reduction in transaction costs: Compared to direct investing in the capital market, investing through the funds is relatively less expensive as the benefit of economies of scale is passed on to the investors.

4. Liquidity: Often, investors cannot sell the securities held easily, while in case of mutual funds, they can easily encash their investment by selling their units to the fund if it is an open-ended scheme or selling them on a stock exchange if it is a close-ended scheme.

5. Convenience: Investing in mutual fund reduces paperwork, saves time and makes investment easy.

6. Flexibility: Mutual funds offer a family of schemes, and investors have the option of transferring their holdings from one scheme to the other.

7. Tax benefits: Mutual fund investors now enjoy income-tax benefits. Dividends received from mutual funds' debt schemes are tax exempt to the overall limit of Rs 9,000 allowed under section 80L of the Income Tax Act.

8. Transparency: Mutual funds transparently declare their portfolio every month. Thus an investor knows where his/her money is being deployed and in case they are not happy with the portfolio they can withdraw at a short notice.

9. Stability to the stock market: Mutual funds have a large amount of funds which provide them economies of scale by which they can absorb any losses in the stock market and continue investing in the stock market. In addition, mutual funds increase liquidity in the money and capital market.

10. Equity research: Mutual funds can afford information and data required for investments as they have large amount of funds and equity research teams available with them.

(D). 3 Types of Mutual Funds:

Functional Classification of Mutual Funds:

1. Open-ended schemes: In case of open-ended schemes, the mutual fund continuously offers to sell and repurchase its units at net asset value (NAV) or NAV-related prices. Unlike close-ended schemes, open-ended ones do not have to be listed on the stock exchange and can also offer repurchase soon after allotment. Investors can enter and exit the scheme any time during the life of the fund. Open-ended schemes do not have a fixed corpus. The corpus of fund may increases or decreases, depending on the purchase or redemption of units by investors. There is no fixed redemption period in open-ended schemes, which can be terminated whenever the need arises. The fund offers a redemption price at which the holder can sell units to the fund and exit. Besides, an investor can enter the fund again by buying units from the fund at its offer price. Such funds announce sale and repurchase prices from time-to-time. UTI's US-64 scheme is an example of such a fund. The key feature of open-ended funds is liquidity. They increase liquidity of the investors as the units can be continuously bought and sold. The investors can develop their income or saving plan due to free entry and exit frame of funds. Open-ended schemes usually come as a family of schemes which enable the investors to switch over from one scheme to another of same family.

2. Close-ended schemes: Close-ended schemes have a fixed corpus and a stipulated maturity period ranging between 2 to 5 years. Investors can invest in the scheme when it is launched. The scheme remains open for a period not exceeding 45 days. Investors in close-ended schemes can buy units only from the market, once initial subscriptions are over and thereafter the units are listed on the stock exchanges where they dm be bought and sold. The fund has no interaction with investors till redemption except for paying dividend/bonus. In order to provide an alternate exit route to the investors, some close-ended funds give an option of selling back the units to the mutual fund through periodic repurchase at NAV related prices. If an investor sells units directly to the fund, he cannot enter the fund again, as units bought back by the fund cannot be reissued. The close-ended scheme can be converted into an open-ended one. The units can be rolled over by the passing of a resolution by a majority of the unit--holders.

3. Interval scheme: Interval scheme combines the features of open-ended and close-ended schemes. They are open for sale or redemption during predetermined intervals at NAVrelated prices. Portfolio Classification Here, classification is on the basis of nature and types of securities and objective of investment. 1. Income funds: The aim of income funds is to provide safety of investments and regular income to investors. Such schemes invest predominantly in income-bearing instruments like bonds, debentures, government securities, and commercial paper. The return as well as the risk are lower in income funds as compared to growth funds.

4. Growth funds: The main objective of growth funds is capital appreciation over the medium-to-long- term. They invest most of the corpus in equity shares with significant growth potential and they offer higher return to investors in the long-term. They assume the risks associated with equity investments. There is no guarantee or assurance of returns. These schemes are usually close-ended and listed on stock exchanges.

5. Balanced funds: The aim of balanced scheme is to provide both capital appreciation and regular income. They divide their investment between equity shares and fixed nicebearing instruments in such a proportion that, the portfolio is balanced. The portfolio of such funds usually comprises of companies with good profit and dividend track records. Their exposure to risk is moderate and they offer a reasonable rate of return.

6. Money market mutual funds: They specialise in investing in short-term money market instruments like treasury bills, and certificate of deposits. The objective of such funds is high liquidity with low rate of return.

Geographical Classification

1. Domestic funds: Funds which mobilise resources from a particular geographical locality like a country or region are domestic funds. The market is limited and confined to the boundaries of a nation in which the fund operates. They can invest only in the securities which are issued and traded in the domestic financial markets.

2. Offshore funds: Offshore funds attract foreign capital for investment in 'the country of the issuing company. They facilitate cross-border fund flow which leads to an increase in foreign currency and foreign exchange reserves. Such mutual funds can invest in securities of foreign companies. They open domestic capital market to international investors. Many mutual funds in India have launched a number of offshore funds, either independently or jointly with foreign investment management companies. The first offshore fund, the India Fund, was launched by Unit Trust of India in July 1986 in collaboration with the US fund manager, Merril Lynch. Others

1. Sectoral: These funds invest in specific core sectors like energy, telecommunications, IT, construction, transportation, and financial services. Some of these newly opened-up sectors offer good investment potential.

2. Tax saving schemes: Tax-saving schemes are designed on the basis of tax policy with special tax incentives to investors. Mutual funds have introduced a number of tax saving schemes. These are close--ended schemes and investments are made for ten years, although investors can avail of encashment facilities after 3 years. These schemes contain various options like income, growth or capital application. The latest scheme offered is the Systematic Withdrawal Plan (SWP) which enables investors to reduce their tax incidence on dividends from as high as 30% to as low as 3 to 4%.

3. Equity-linked savings scheme (ELSS): In order to encourage investors to invest in equity market, the government has given tax-concessions through special schemes. Investment in these schemes entitles the investor to claim an income tax rebate, but these schemes carry a lock-in period before the end of which funds cannot be withdrawn.

4. Special schemes: Mutual funds have launched special schemes to cater to the special needs of investors. UTI has launched special schemes such as Children's Gift Growth Fund, 1986, Housing Unit Scheme, 1992, and Venture Capital Funds.

5. Gilt funds: Mutual funds which deal exclusively in gilts are called gilt funds. With a view to creating a wider investor base for government securities, the Reserve Bank of India encouraged setting up of gilt funds. These funds are provided liquidity support by the Reserve Bank.

6. Load funds: Mutual funds incur certain expenses such as brokerage, marketing expenses, and communication expenses. These expenses are known as 'load' and are recovered by the fund when it sells the units to investors or repurchases the units from withholders. In other words, load is a sales charge, or commission, assessed by certain mutual funds to cover their selling costs. Loads can be of two types-Front-end-load and back-endload. Front-end-load, or sale load, is a charge collected at the time when an investor enters into the scheme. Back-end, or repurchase, load is a charge collected when the investor gets out of the scheme. Schemes that do not charge a load are called 'No load' schemes.

7. Index funds: It is a mutual fund which invests in securities in the index on which it is based BSE Sensex or S&P CNX Nifty. It invests only in those shares which comprise the market index and in exactly the same proportion as the companies/weightage in the index. So that the value of such index funds varies with the market index. An index fund follows a passive investment strategy as no effort is made by the fund manager to identify stocks for investment/dis-investment. The fund manager has to merely track the index on which it is based. His portfolio will need an adjustment in case there is a revision in the underlying index. In other words, the fund manager has to buy stocks which are added to the index and sell stocks which are deleted from the index.

8. PE ratio fund: PE ratio fund is another mutual fund variant that is offered by Pioneer IT! Mutual Fund. The PE (Price-Earnings) ratio is the ratio of the price of the stock of a company to its earnings per share (EPS). The PE ratio of the index is the weighted average price-earnings ratio of all its constituent stocks. The PE ratio fund invests in equities and debt instruments wherein the proportion of the investment is determined by the ongoing price-earnings multiple of the market. The objective of this scheme is to provide superior risk-adjusted returns through a balanced portfolio of equity and debt instruments.

9. Exchange traded funds: Exchange Traded Funds (ETFs) are a hybrid of open-ended mutual funds and listed individual stocks. They are listed on stock exchanges and trade like individual stocks on the stock exchange. However, trading at the stock exchanges does not affect their portfolio. ETFs do not sell their shares directly to investors for cash. The shares are offered to investors over the stock exchange. ETFs are basically passively managed funds that track a particular index such as S&P CNX Nifty. Since they are listed on stock exchanges, it is possible to buy and sell them throughout the day and their price is determined by the demand-supply forces in the market. In practice, they trade in a small range around the value of the assets (NAV) held by them. ETFs offer several distinct advantages. ·ETFs bring the trading and real time pricing advantages of individual stocks to mutual funds. The ability to trade intraday at prices that are usually close to the actual intra-day NAV of the scheme makes it almost real-time trading. ·ETFs are simpler to understand and hence they can attract small investors who are deterred to trade in index futures due to requirement of minimum contract size. Small investors can buy minimum one unit of ETF, can place limit orders and trade intra-day. This, in turn, would increase liquidity of the cash market. ·ETFs can be used to arbitrate effectively between index futures and spot index. ·ETFs provide the benefits of diversified index funds. The investor can benefit from the flexibility of stocks as well as the diversification.

(D). 4 Objectives of AMFI

The Association of Mutual Funds in India (AMFI) is devoted to developing the Indian Mutual Fund Industry on professional, healthy and ethical ways and to enhance and maintain standards in all areas with a view to protecting and promoting the interests of mutual funds and their unit holders. In other word, AMFI is a dedicated regulating authority established to protect mutual fund investors' interests and maintain the industry's proper functioning. It is a non-profit organization in the Mutual Funds sector under SEBI. Since its incorporation in 1995, it has set various regulations to maintain ethics and transparency in the Mutual Fund industry for Indian investors.

Objectives of AMFI

AMFI has been incorporated with several objectives; some of them are given below.

1. To define professional and ethical standards to be followed in the Mutual Fund sector.
2. To interact with the SEBI and report to them on all matters concerning the Mutual Fund industry.
3. To represent all the regulatory bodies on all matters relating to the Mutual Fund industry.

4. To assist in policing distributor behavior, including sanctions (cancellation of ARN) for Code of Conduct infractions.

5. To enhance financial literacy and help in increasing accessibility and transparency of investments to draw in additional investors.

6. To assist in defending both the interests of asset management firms and Indian investors.

For the fulfillment of all its objectives, AMFI has formed several committees to delegate responsibilities. It includes, Financial Literacy Committee, Certified Distributors (ARN) Committee, Operations, Compliance and Risk Committee, Valuation Committee, Equity Committee etc. Now a day, mutual funds have become a popular investment option amongst Indian investors. Thus, an establishment objective of AMFI is to protect and promote the interest of investors. It acts as a watchdog of the Indian Mutual Fund industry that not only protects investors but also promotes investments in mutual funds. Even though AMFI is here to protect you, as an investor, you should also be cautious and always check the entity's credibility before investing.

1.4 Summary:

In this unit we studied the Indian capital market comprising primary and secondary capital market, its concepts, online procedure and functions socio-economic development of the country. Indian capital market fulfills the requirement of medium and long term loans to trading and business organization. It is perform the functions such as collecting savings and consolidating them, raising capital for industries, providing opportunities for investment, expanding and using modern techniques for trade which helps the development of various sectors as well as economic development of country. The institutions which demand and supply the long term loans come together in the capital market. The primary market is the part of the capital market that deals with issuing of new securities, creates long term instruments through which corporate entities raise funds from the capital market. The investor purchases the new securities via an investment bank or lead bank or merchant bankers. The major role of the primary capital market is to facilitate capital growth by enabling individuals to convert savings into investments. Moreover, the significance of stock exchange is found in its operation of smooth marketability and liquidity of corporate securities. It provides ready market for

buying and selling of corporate securities. This market creates an image for a company. It facilitates the self assessment of financial status of the corporate enterprise and provides capital formation and promotes industrial growth of the country by attracting investment from the general public.

Now a day's many schemes have been planned for the development of capital market such as, formation of SEBI, improvement in share market, establishment of credit rating agencies etc. The overall objectives of SEBI are to protect the interest of investors and to promote the development of stock exchange and to regulate the activities of stock market. Apart from that, credit rating and depository are the important aspects of capital market, Credit rating plays vital role in financial market by helping to reduce the information asymmetric between lenders and investors. It provides ancillary business services and other services like risk management and consulting services to help financial institutions to manage credit and operational risks. The role of depository system is not only maintaining the accounts of the shareholder but to undertake and collect dividends, bonus shares, etc., on behalf of the shareholder. Periodically, the shareholders have informed of their holdings by a Depository agent through a statement of accounts. Any sale or purchase of shares have take place through the Depository. Thus, the capital market of India was not developed before independence. But considering the importance of capital market in economic development, major steps were taken for the development of capital market. There is an increase in participating institutions of capital market. But lack of sufficient investment, less involvement in agriculture sector are some the limitation of capital market.

1.5 Terms to Remember

1. **India capital market-** It is a financial market where long-term debt or equity-backed securities are bought and sold. Suppliers are people/organizations with the capital to lend or invest.
2. **Primary Market-** The primary market is the part of the capital market that deals with issuing of new securities.
3. **Underwriting of Securities-** It is the process by which investment banks raise investment capital from investors on behalf of corporations and governments that are issuing securities.

4. **Greenshoe Option:** Over-allotment options are known as greenshoe option. A greenshoe option provides additional price stability to a security issue because the underwriter can increase supply and smooth out price fluctuations**.**

5. **Securities Market-** It is known as stock exchange in Britain. In such market, long term securities like shares and debentures are transacted. It is a secondary market.

6. **Financial instruments-** Instruments against which loans are extended are called financial instruments. E.g. deposit certificate, securities etc.

7. **Underwriting-** It is the process that a lender or other financial service uses to assess the credit worthiness or risk of a potential customer.

8. **Stock Market-** It is a capital market where long term finance for the development of companies can be obtained by selling the securities through authorized persons.

9. **Stock Broker-** A person who assist the investors in buying and selling of securities in the secondary market. The trading activity takes place between investor through the intermediaries called stock brokers.

10. **Investor-** The person or institution purchasing financial instruments like shares and debentures. Such investment is made in money terms.

11. **Credit Rating-** Means an evaluation of debtors' credit ability, in relation to particular liability in present circumstances.

12. **Depository-** It is an organization which holds securities (like shares, debentures, bonds, government securities, mutual fund units etc.) of investors in electronic form at the request of the investors through a registered Depository Participant. It can be compared to a bank. It provides services related to transactions in securities.

13. **Underwriter-** Underwriter gives guarantee of the collecting certain amount by selling equality shares of the company before a particular day. If the shares are not sold before the particular day, the underwriter purposes these shares.

14. **Mutual Fund:** It is a financial intermediary that pools the savings of investors for collective investment.

15. **Association of Mutual Funds in India (AMFI):** It is a dedicated regulating authority established to protect mutual fund investors' interests and maintain the industry's proper functioning.

1.6 Check Your Progress

A. Choose the correct alternative:

1. Indian Capital Market is divided in organized and -------------

   a. Unorganized b. Developed

   c. Mixed d. All of above

2. The first organized stock exchange in India was started in -------------

   a. Calcutta b. Mumbai (Bombay)

   c. Chennai (Madras) d. Ahmedabad

3. What is full form of SEBI?

   a. Sale and Exchange Body and Industry

   b. Staff of Executive body of India

   c. Securities and Exchange Board of India

   d. Selection of Enterprise Board of India.

4. Mechanism through which there is exchange of medium and long term loans is called--------

   a. Money Market b. Capital Market

   c. Loans Market d. Currency Market

5. In capital market the demand for capital comes from ---------

   a. Public undertaking b. Social System

   c. Both d. None of the above

6. To avoid the frauds that takes place in Capital Market-------was established.

   a. NABARD b. UTI c. SEBI d. SBI

7. Securities Contracts Act, -------has specified the trading mechanism of the Stock Exchange.

a. 1946 b. 1976 c. 1956 d. 1986

8. Investment Information and Credit Rating Agency of India Limited (ICRA) was established in the year -------

   a. 1981 b. 2001 c. 1971 d. 1991

9. Fitch Ratings Limited is one of the good rating agency in India, which is ------- owned subsidiary of a foreign company.

   a. 50% b. 49% c. 100% d. 51%

10. The Securities and Exchange Board of India has granted registration for ------- depositories in India

    a. two b. three c. five d. ten

11. .... is known as a collective investment vehicle

    a) Venture Capital b) Equity Share c) Mutual Fund d) Debenture

B. Fill in the Blanks:

i) Capital Market fulfils ---------------

ii) The primary capital market is deals with issuing of ---------- securities.

iii) Private Foreign banks are ------- registered with SEBI.

iv) The services of an underwriter are typically used during a ---------in a primary market.

v) -----------assist the investors in buying and selling of securities in the secondary market.

vi) The CRISIL is established in the year ---------.

vii) National Securities Depository Limited (NSDL) is the --------- depository set up in India.

viii) A fund is ------ as all of its returns, minus its expenses, are shared by the fund's investors.

C. State 'True' or 'False'.

i. In India, there is much need of control of the securities market.

ii. Investors get safety in depository system.

iii. There is no existence of unorganized sector in the Indian Capital Market.

iv. Over-allotment options are known as greenshoe option

v. Depository Participant is not provides the service of opening a demat account to the investor.

vi. All investors can keep their investment in intangibles. .

vii. SEBI has control over Merchant Bank.

viii. NSDL depository has promoted by institutions of national importance responsible for economic development of the country.

1.7 Answers to Check Your Progress

A. Choose the correct alternative:

1 – a, 2 – b, 3 – c, 4 – b, 5 – b, 6 – c, 7 – c, 8 – d, 9 – c, 10 – a, 11-c

B. Fill in the Blanks:

i- Fixed capital requirement, ii- new, iii-not, iv- public offering,

v- Stock brokers, vi- 1987, vii- first and largest, viii-Mutual

C. State 'True' or 'False'.

i- True, ii- True, iii-False, iv- True v- False vi- False, vii- True, viii True

1.8 Exercise

1. Explain the concept of Indian Capital Market.
2. What is primary capital market? State its functions.
3. Describe the methods of selling corporate securities in primary capital market.
4. Explain the concept of Greenshoe Option.
5. State the difference between the IPO and FPO
6. Define the stock market. State its role and functions.
7. Describe the role of SEBI in regulating capital markets in India.
8. Describe the online trading procedure on a stock exchange.
9. What is credit rating? Describe the credit rating agencies in India.

10. State the meaning of Depository. Explain its benefits.
11. Explain the Concept of National Securities Depository Limited (NSDL) and Central Depository Service Limited (CDSL).
12. State the role of Depository in India.
13. Explain the Concept of Mutual Funds and its types.
14. Describe the Importance of Mutual Funds
15. State the objectives of AMFI

1.9 Further Readings

1. Fundamentals of the Indian Financial System – Vasant Desai.
2. Financial Management - Prasanna Chandra
3. Banks and Institutional Management: A New Orientation- Vasant Desai.
4. Financial Management - Khan and Jain
5. Indian Economy – Recent Edition- Rudra Dutta and K.P.M Sundaram
6. Investment and Securities Markets in India- V. A. Avadhani
7. India's Banking and Financial Sector in the New Millennium, Ghaziabad, Academic Foundation, 2001

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Unit-2

Portfolio Management, Financial Inclusion and Micro Finance

Unit Structure

2.0 Objectives:

After studying this unit, the students will be able to:

- Understand the concept of mutual fund, its types and present position of mutual funds in India.
- Know the meaning and objectives of portfolio management and issues in portfolio construction.
- Understand the concept, need and policy about financial inclusion.
- Know the concept need and present position of microfinance in India

2.1 Introduction:

Financial sector is going through a phase where lot of new products, services are coming into the market. People, in general, feel that investment in stock market has a huge risk. In order to cope up with the requirement of diversification, liquidity and low risk; mutual fund evolved as an investment avenue. This facilitates lot of advantages to a small investor. Further, those who wish to invest their money and are able to share the profit can avail benefit of port-folio management where huge funds are given to fund managers who professionally manage the funds. On the other hand, there are people who do not have even access to basic banking services. It is important to bring them into mainstream for which financial inclusion drive is necessary. Micro finance is one of the way through which the needy people are provided financial services at affordable cost. This chapter throws light on the important issues emerging in financial sector today.

2.2 Presentation of Subject Matter:

2.2.1 Part A: Mutual Fund: Concept, Importance, Types and Present Position

2.2.1.1 Introduction:

A mutual fund is a financial intermediary that pools the savings of investors for collective investment in a diversified portfolio of securities. A fund is “mutual” as all of its returns, minus its expenses, are shared by the fund’s investors. The Securities and Exchange Board of India (Mutual Funds) Regulations, 1996 defines a mutual fund as a ‘a fund established in the form of a trust to raise money through the sale of units to the public or a section of the public under one or more schemes for investing in securities, including money market instruments’. According to the above definition, a mutual fund in India can raise resources through sale of units to the public. It can be set up in the form of a Trust under the Indian Trust Act. The definition has been further extended by allowing mutual funds to diversify their activities in the following areas: Portfolio management services, Management of offshore funds, Providing advice to offshore funds, Management of pension or provident funds, Management of venture capital funds, Management of money market funds, Management of real estate funds.

A mutual fund serves as a link between the investor and the securities market by mobilising savings from the investors and investing them in the securities market to generate returns. Thus, a mutual fund is akin to portfolio management services (PMS). Although, both are conceptually same, they are different from each other. Portfolio management services are offered to high net worth individuals; taking into account their risk profile, their investments are managed separately. In the case of mutual funds, savings of small investors are pooled under a scheme and the returns are distributed in the same proportion in which the investments are made by the investors/unit-holders. Mutual fund is a collective savings scheme. Mutual funds play an important role in mobilising the savings of small investors and channelising the same for productive ventures in the Indian economy. **Benefits of Mutual Funds** An investor can invest directly in individual securities or indirectly through a financial intermediary. Globally, mutual funds have established themselves as the means of investment for the retail investor.

1. Professional management: An average investor lacks the knowledge of capital market operations and does not have large resources to reap the benefits of investment. Hence, he requires the help of an expert. It, is not only expensive to 'hire the services' of an expert but it is more difficult to identify a real expert. Mutual funds are managed by professional managers who have the requisite skills and experience to analyse the performance and prospects of companies. They make possible an organised investment strategy, which is hardly possible for an individual investor.

2. Portfolio diversification: An investor undertakes risk if he invests all his funds in a single scrip. Mutual funds invest in a number of companies across various industries and sectors. This diversification reduces the riskiness of the investments.

3. Reduction in transaction costs: Compared to direct investing in the capital market, investing through the funds is relatively less expensive as the benefit of economies of scale is passed on to the investors.

4. Liquidity: Often, investors cannot sell the securities held easily, while in case of mutual funds, they can easily encash their investment by selling their units to the fund if it is an open-ended scheme or selling them on a stock exchange if it is a close-ended scheme.

5. Convenience: Investing in mutual fund reduces paperwork, saves time and makes investment easy.

6. Flexibility: Mutual funds offer a family of schemes, and investors have the option of transferring their holdings from one scheme to the other.

7. Tax benefits Mutual fund investors now enjoy income-tax benefits. Dividends received from mutual funds' debt schemes are tax exempt to the overall limit of Rs 9,000 allowed under section 80L of the Income Tax Act.

8. Transparency Mutual funds transparently declare their portfolio every month. Thus an investor knows where his/her money is being deployed and in case they are not happy with the portfolio they can withdraw at a short notice.

9. Stability to the stock market Mutual funds have a large amount of funds which provide them economies of scale by which they can absorb any losses in the stock market and continue investing in the stock market. In addition, mutual funds increase liquidity in the money and capital market.

10. Equity research Mutual funds can afford information and data required for investments as they have large amount of funds and equity research teams available with them. History of Mutual Funds The history of mutual funds, dates back to 19th century Europe, in particular, Great Britain. Robert Fleming set up in 1868 the first investment trust called Foreign and Colonial Investment Trust which promised to manage the finances of the moneyed classes of Scotland by spreading the investment over a number of different stocks. This investment trust and other investment trusts which were subsequently set up in Britain and the US, resembled today's close-ended mutual funds. The first mutual fund in the US, Massachusetts Investors' Trust, was setup in March 1924. This was the first open-ended mutual fund. The stock market crash in 1929, the Great Depression, and the outbreak of the Second World War slackened the pace of growth of the mutual fund industry. Innovations in products and services increased the popularity of mutual funds in the 1950s and 1960s. The first international stock mutual fund was introduced in the US in 1940. In 1976, the first tax-exempt municipal bond funds emerged and in 1979, the first money market mutual funds were created. The latest additions are the international bond fund in 1986 and arm funds in 1990. This industry witnessed substantial growth in the eighties and nineties when there was a significant increase in the number of mutual funds, schemes, assets, and shareholders. In the US, the mutual fund industry

registered a ten fold growth in the eighties (1980-89) only, with 25% of the household sector's investment in financial assets made through them. Fund assets increased from less than $150 billion in 1980 to over $4 trillion by the end of 1997. Since 1996, mutual fund assets have exceeded bank deposits. The mutual fund industry and the banking industry virtually rival each other in size.

Growth of Mutual Funds in India : The Indian mutual fund industry has evolved over distinct stages. The growth of the mutual fund industry in India can be divided into four phases:

Phase I (1964-87), Phase II (1987-92), Phase III (1992-97), and Phase IV (beyond 1997).

Phase I: The mutual fund concept was introduced in India with the setting up of UTI in 1963. The Unit Trust of India (UTI) was the first mutual fund set up under the UTI Act, 1963, a special act of the Parliament. It became operational in 1964 with a major objective of mobilising savings through the sale of units and investing them in corporate securities for maximising yield and capital appreciation. This phase commenced with the launch of Unit Scheme 1964 (US-64) the first open-ended and the most popular scheme. UTI's investible funds, at market value (and including the book value of fixed assets) grew from Rs 49 crore in1965 to Rs 219 crore in 1970-71 to Rs 1,126 crore in 1980-81 and further to Rs 5,068 crore by June 1987. Its investor base had also grown to about 2 million investors. It launched innovative schemes during this phase. Its fund family included five income-oriented, open-ended schemes, which were sold largely through its agent network built up over the years. Master share, the equity growth fund launched in 1986, proved to be a grand marketing success. Master share was the first real close-ended scheme floated by UTI. It launched India Fund in 1986-the first Indian offshore fund for overseas investors, which was listed on the London Stock Exchange (LSE). UTI maintained its monopoly and experienced a consistent growth till 1987.

Phase II: The second phase witnessed the entry of mutual fund companies sponsored by nationalised banks and insurance companies. In 1987, SBI Mutual Fund and Canbank Mutual Fund were set up as trusts under the Indian Trust Act, 1882. In 1988, UTI floated another offshore fund, namely, The India Growth Fund which was listed on the New York Stock Exchange (NYSE). By 1990, the two nationalised insurance giants, LIC and GIC, and nationalised banks, namely, Indian

Bank, Bank of India, and Punjab National Bank had started operations of wholly-owned mutual fund subsidiaries. The assured return type of schemes floated by the mutual funds during this phase were perceived to be another banking product offered by the arms of sponsor banks. In October 1989, the first regulatory guidelines were issued by the Reserve Bank of India, but they were applicable only to the mutual funds sponsored by FIIs. Subsequently, the Government of India issued comprehensive guidelines in June 1990 covering all ‘mutual funds. These guidelines emphasised compulsory registration with SEBI and an arms length relationship be maintained between the sponsor and asset management company (AMC). With the entry of public sector funds, there was a tremendous growth in the size of the mutual fund industry with investible funds, at market value, increasing to Rs 53,462 crore and the number of investors increasing to over 23 million. The buoyant equity markets in 1991-92 and tax benefits under equity-linked savings schemes enhanced the attractiveness of equity funds.

Phase III: The year 1993 marked a turning point in the history of mutual funds in India. Tile Securities and Exchange Board of India (SEBI) issued the Mutual Fund Regulations in January 1993. SEBI notified regulations bringing all mutual funds except UTI under a common regulatory framework. Private domestic and foreign players were allowed entry in the mutual fund industry. Kothari group of companies, in joint venture with Pioneer, a US fund company, set up the first private mutual fund the Kothari Pioneer Mutual Fund, in 1993. Kothari Pioneer introduced the first open-ended fund Prima in 1993. Several other private sector mutual funds were set up during this phase. UTI launched a new scheme, Master-gain, in May 1992, which was a phenomenal success with a subscription of Rs 4,700 crore from 631akh applicants. The industry’s investible funds at market value increased to Rs 78,655 crore and the number of investor accounts increased to 50 million. However, the year 1995 was the beginning of the sluggish phase of the mutual fund industry. During 1995 and 1996, unit holders saw an erosion in the value of their investments due to a decline in the NA V s of the equity funds. Moreover, the service quality of mutual funds declined due to a rapid growth in the number of investor accounts, and the inadequacy of service infrastructure. A lack of performance of the public sector funds and miserable failure of foreign funds like Morgan Stanley eroded the confidence of investors in fund managers. Investors perception about mutual funds, gradually turned negative. Mutual funds found it increasingly difficult to raise money. The average annual sales declined from about Rs13,000 . crore in 1991-94 to about Rs 9,000 crore in 1995 and 1996.

Phase IV: During this phase, the flow of funds into the kitty of mutual funds sharply increased. This significant growth was aided by a more positive sentiment in the capital market, significant tax benefits, and improvement in the quality of investor service. Investible funds, at market value, of the industry rose by June 2000 to over Rs 1,10,000 crore with UTI having 68% of the market share. During 1999-2000 sales mobilisation reached a record level of Rs 73,000 crore as against Rs 31,420 crore in the preceding year. This trend was, however, sharply reversed in 2000-01. The UTI dropped a bombshell on the investing public by disclosing the NAV of US-64-its flagship scheme as on December 28,2000, just at Rs 5.81 as against the face value of Rs 10 and the last sale price of Rs 14.50. The disclosure of NAV of the country's largest mutual fund scheme was the biggest shock of the year to investors. Crumbling global equity markets, a sluggish economy coupled with bad investment decisions made life tough for big funds across the world in 2001-02. The effect of these problems was felt strongly in India also. Pioneer m, JP Morgan and Newton Investment Management pulled out from the Indian market. Bank of India MF liquidated all its schemes in 2002. The Indian mutual fund industry has stagnated at around Rs 1,00,000 crore assets since 2000-01. This stagnation is partly a result of stagnated equity markets and the indifferent performance by players. As against this, the aggregate deposits of Scheduled Commercial Banks (SCBs) as on May 3, 2002, stood at Rs 11,86,468 crore. Mutual funds assets under management (AUM) form just around 10% of deposits of SCBs. The Unit Trust of India is losing out to other private sector players. While there has been an increase in AUM by around 11% during the year 2002, UTI on the contrary has lost more than 11% in AUM. The private sector mutual funds have benefited the most from the debacle ofUS-64 of UTI. The AUM of this sector grew by around- 60% for the year ending March 2002. Types of Mutual Fund Schemes The objectives of mutual funds are to provide continuous liquidity and higher yields with high degree of safety to investors. Based on these objectives, different types of mutual fund schemes have evolved.

2.2.1.2 Types of Mutual Fund Schemes :

Functional Classification of Mutual Funds:

1. Open-ended schemes: In case of open-ended schemes, the mutual fund continuously offers to sell and repurchase its units at net asset value (NAV) or NAV-related prices. Unlike close-ended schemes, open-ended ones do not have to be listed on the stock exchange and can also offer repurchase soon after allotment. Investors can enter and exit the scheme any time during the life of the fund. Open-ended schemes do not have a fixed corpus. The corpus of fund increases or decreases, depending on the purchase or redemption of units by investors. There is no fixed redemption period in open-ended schemes, which can be terminated whenever the need arises. The fund offers a redemption price at which the holder can sell units to the fund and exit. Besides, an investor can enter the fund again by buying units from the fund at its offer price. Such funds announce sale and repurchase prices from time-to-time. UTI's US-64 scheme is an example of such a fund. The key feature of open-ended funds is liquidity. They increase liquidity of the investors as the units can be continuously bought and sold. The investors can develop their income or saving plan due to free entry and exit frame of funds. Open-ended schemes usually come as a family of schemes which enable the investors to switch over from one scheme to another of same family.

2. Close-ended schemes: Close-ended schemes have a fixed corpus and a stipulated maturity period ranging between 2 to 5 years. Investors can invest in the scheme when it is launched. The scheme remains open for a period not exceeding 45 days. Investors in close-ended schemes can buy units only from the market, once initial subscriptions are over and thereafter the units are listed on the stock exchanges where they dm be bought and sold. The fund has no interaction with investors till redemption except for paying dividend/bonus. In order to provide an alternate exit route to the investors, some close-ended funds give an option of selling back the units to the mutual fund through periodic repurchase at NAV related prices. If an investor sells units directly to the fund, he cannot enter the fund again, as units bought back by the fund cannot be reissued. The close-ended scheme can be converted into an open-ended one. The units can be rolled over by the passing of a resolution by a majority of the unit--holders.

3. Interval scheme: Interval scheme combines the features of open-ended and close-ended schemes. They are open for sale or redemption during predetermined intervals at NAVrelated prices. Portfolio Classification Here, classification is on the basis of nature and types of securities and objective of investment. 1. Income funds:

The aim of income funds is to provide safety of investments and regular income to investors. Such schemes invest predominantly in income-bearing instruments like bonds, debentures, government securities, and commercial paper. The return as well as the risk are lower in income funds as compared to growth funds.

Growth funds: The main objective of growth funds is capital appreciation over the medium-to-long- term. They invest most of the corpus in equity shares with significant growth potential and they offer higher return to investors in the long-term. They assume the risks associated with equity investments. There is no guarantee or assurance of returns. These schemes are usually close-ended and listed on stock exchanges.

3. Balanced funds: The aim of balanced scheme is to provide both capital appreciation and regular income. They divide their investment between equity shares and fixed nicebearing instruments in such a proportion that, the portfolio is balanced. The portfolio of such funds usually comprises of companies with good profit and dividend track records. Their exposure to risk is moderate and they offer a reasonable rate of return.

4. Money market mutual funds: They specialise in investing in short-term money market instruments like treasury bills, and certificate of deposits. The objective of such funds is high liquidity with low rate of return.

Geographical Classification

1. Domestic funds: Funds which mobilise resources from a particular geographical locality like a country or region are domestic funds. The market is limited and confined to the boundaries of a nation in which the fund operates. They can invest only in the securities which are issued and traded in the domestic financial markets.

2. Offshore funds: Offshore funds attract foreign capital for investment in ‘the country of the issuing company. They facilitate cross-border fund flow which leads to an increase in foreign currency and foreign exchange reserves. Such mutual funds can invest in securities of foreign companies. They open domestic capital market to international investors. Many mutual funds in India have launched a number of offshore funds, either independently or jointly with foreign investment management companies. The first offshore fund, the India Fund, was launched by Unit Trust of India in July 1986 in collaboration with the US fund manager, Merril Lynch. Others

1. Sectoral: These funds invest in specific core sectors like energy, telecommunications, IT, construction, transportation, and financial services. Some of these newly opened-up sectors offer good investment potential.

2. Tax saving schemes: Tax-saving schemes are designed on the basis of tax policy with special tax incentives to investors. Mutual funds have introduced a number of tax saving schemes. These are close--ended schemes and investments are made for ten years, although investors can avail of encashment facilities after 3 years. These schemes contain various options like income, growth or capital application. The latest scheme offered is the Systematic Withdrawal Plan (SWP) which enables investors to reduce their tax incidence on dividends from as high as 30% to as low as 3 to 4%.

3. Equity-linked savings scheme (ELSS): In order to encourage investors to invest in equity market, the government has given tax-concessions through special schemes. Investment in these schemes entitles the investor to claim an income tax rebate, but these schemes carry a lock-in period before the end of which funds cannot be withdrawn.

4. Special schemes: Mutual funds have launched special schemes to cater to the special needs of investors. UTI has launched special schemes such as Children's Gift Growth Fund, 1986, Housing Unit Scheme, 1992, and Venture Capital Funds.

5. Gilt funds: Mutual funds which deal exclusively in gilts are called gilt funds. With a view to creating a wider investor base for government securities, the Reserve Bank of India encouraged setting up of gilt funds. These funds are provided liquidity support by the Reserve Bank.

6. Load funds: Mutual funds incur certain expenses such as brokerage, marketing expenses, and communication expenses. These expenses are known as 'load' and are recovered by the fund when it sells the units to investors or repurchases the units from withholders. In other words, load is a sales charge, or commission, assessed by certain mutual funds to cover their selling costs. Loads can be of two types-Front-end-load and back-endload. Front-end-load, or sale load, is a charge collected at the time when an investor enters into the scheme. Back-end, or repurchase, load is a charge collected when the investor gets out of the scheme. Schemes that do not charge a load are called 'No load' schemes. In other words, if the asset management company (AMC) bears the load during the initial launch of the scheme, then these schemes are known as no-load schemes. However, these no-load schemes can have an exit load when the unit holder gets out of the scheme before a stipulated period mentioned in the initial offer. This is done to prevent short-term investments and redemptions. Some funds may also charge different amount of loads to investors depending upon the time period the investor has stayed with the funds. The longer the investor stays with the fund, less is the amount of exit load charged. This is known as contingent deferred sales' charge (CDSL). It is a back-end (exit load) fee imposed by certain funds on shares redeemed with a specific period following their purchase and is usually assessed on a sliding scale.

7. Index funds: An index fund is a mutual fund which invests in securities in the index on which it is based BSE Sensex or S&P CNX Nifty. It invests only in those shares which comprise the market index and in exactly the same proportion as the companies/weightage in the index so that the value of such index funds varies with the market index. An index fund follows a passive investment strategy as no effort is made by the fund manager to identify stocks for investment/dis-investment. The fund manager has to merely track the index on which it is based. His portfolio will need an adjustment in case there is a revision in the underlying index. In other words, the fund manager has to buy stocks which are added to the index and sell stocks which are deleted from the index. Internationally, index funds are very popular. Around onethird of professionally run portfolios in the US are index funds. Empirical evidence points out that active fund managers have not been able to perform well. Only 20-25% of actively managed equity mutual funds out-perform benchmark indices in the long-term. These active fund managers park 80% of their money in an index and do active management on the remaining 20%. Moreover, risk averse investors like provident funds and pension funds prefer investment in passively managed funds like index funds.

8. PE ratio fund: PE ratio fund is another mutual fund variant that is offered by Pioneer IT! Mutual Fund. The PE (Price-Earnings) ratio is the ratio of the price of the stock of a company to its earnings per share (EPS). The PE ratio of the index is the weighted average price-earnings ratio of all its constituent stocks. The PE ratio fund invests in equities and debt instruments wherein the proportion of the investment is determined by the ongoing price-earnings multiple of the market. Broadly, around 90% of the investible funds will be invested in equity if the Nifty Index PE ratio is 12 or below. If this ratio exceeds 28, the investment will be in debt/money markets. Between the two ends of 12 and 28 PIE ratio of the Nifty, the fund will allocate varying proportions of its investible funds to equity and debt. The objective of this scheme is to provide superior risk-adjusted returns through a balanced portfolio of equity and debt instruments.

9. Exchange traded funds: Exchange Traded Funds (ETFs) are a hybrid of open-ended mutual funds and listed individual stocks. They are listed on stock exchanges and trade like individual stocks on the stock exchange. However, trading at the stock exchanges does not affect their portfolio. ETFs do not sell their shares directly to investors for cash. The shares are offered to investors over the stock exchange. ETFs are basically passively managed funds that track a particular index such as S&P CNX Nifty. Since they are listed on stock exchanges, it is possible to buy and sell them throughout the day and their price is determined by the demand-supply forces in the market. In practice, they trade in a small range around the value of the assets (NAV) held by them. ETFs offer several distinct advantages. ·ETFs bring the trading and real time pricing advantages of individual stocks to mutual funds. The ability to trade intraday at prices that are usually close to the actual intra-day NAV of the scheme makes it almost real-time trading. ·ETFs are simpler to understand and hence they can attract small investors who are deterred to trade in index futures due to requirement of minimum contract size. Small investors can buy minimum one unit of ETF, can place limit orders and trade intra-day. This, in turn, would increase liquidity of the cash market. ·ETFs can be used to arbitrate effectively between index futures and spot index. ·ETFs provide the benefits of diversified index funds. The investor can benefit from the flexibility of stocks as well as the diversification. ·ETFs being passively managed, have somewhat higher NAV against an index fund of the same portfolio. The operating expenses of ETFs are lower than even those of similar index funds as they do not have to service investors who deal in shares through stock exchanges. ·ETFs can be beneficial for financial institutions also. Financial institutions can use ETFs for utilizing idle cash, managing redemptions, modifying sector allocations, and hedging market exposure. The first exchange traded fund-Standard and Poor's Depository Receipt (SPDR-also called Spider)-was launched in the US in 1993. ETFs have grown rapidly with around US$100 billion in assets as on December 2001. Today, about 60% of trading value on the American Stock Exchange (AMEX) is from ETFs. ETFs were launched in Europe and Asia in 2001. Currently, more than 120 ETFs are available in US, Europe, Singapore, Hongkong, Japan, and other countries. Among the popular ones are SPDRs (Spiders) based on the S&P 500 Index, QQQs (cubes) based on the Nasdaq-100 Index, i SHARES based on MSCI Indices and TRAHK (Tracks) based on the Hang Seng Index. The ETF structure has seen over $120 bn pouring into it in more than 220 funds. It has become the fastest growing fund structure. In year 2001 alone, the number of funds doubled from 100 to 200. The first ETF to be introduced in India is Nifty Bench mark Exchange-Traded Scheme (Nifty BeES). It is an open-ended ETF, launched towards the end of 2001 by Benchmark Mutual Funds. The fund is listed in the capital market segment of the NSE and trades the S&P CNX Nifty Index. The Benchmark Asset Management Company has become the first company in Asia (excluding Japan) to introduce ETF.

Net Asset Value (NAV): The net asset value of a fund is the market value of the assets minus the liabilities on the day of valuation. In other words, it is the amount which the shareholders will collectively get if the fund is dissolved or liquidated. The net asset value of a unit is the net asset value of fund divided by the number of outstanding units. Thus NAV = Market Price of Securities + Other Assets - Total Liabilities + Units Outstanding as at the NAV date. NAV = Net Assets of the Scheme + Number of units outstanding, that is, Market value of investments + Receivables + Other Accrued Income + Other Assets - Accrued Expenses - Other Payables - Other Liabilities + No. of units outstanding as at the NAV date. A fund's NAV is affected by four sets of factors: purchase and sale of investment securities, valuation of all investment securities held, other assets and liabilities, and units sold or redeemed. SEBI has issued guidelines on valuation of traded securities, thinly traded securities and non-traded securities. These guidelines were issued to streamline the procedure of calculation of NAV of the schemes of mutual funds. The aggregate value of illiquid securities as defined in the guidelines shall not exceed 15% of the total assets of the scheme and any illiquid securities held above 15% of the total assets shall be valued in the manner as specified in the guidelines issued by the SEBI. Where income receivables on investments has accrued but has not been received for the period specified in the guidelines issued by SEBI, provision shall be made by debiting to the revenue account the income so accrued in the manner specified by guidelines issued by SEBI.

Mutual funds are required to declare their NAV s and sale repurchase prices of all schemes updated daily on regular basis on the AMFI website by 8.00 p.m. and declare NAVs of their close-ended schemes on every Wednesday. According to SEBI (Mutual Funds) (Second Amendment) Regulations, 2000, a mutual fund can now invest up to 5% of its NAV in the unlisted equity shares or equity related instruments in case of open-ended schemes; while in case of close-ended schemes, the mutual fund can now invest up to 10% of its NAV. Mutual Fund Investors Mutual funds in India are open to investment by a. Residents including ·Resident Indian Individuals, including high net worth individuals and the retail or small investors. Indian Companies ·Indian Trusts/Charitable Institutions ·Banks ·Non-Banking Finance Companies ·Insurance Companies ·Provident Funds b. Non-Residents, including ·Non-Resident Indians ·Other Corporate Bodies (OCBs) c. Foreign entities, namely, Foreign Institutional Investors (FIIs) registered with SEBI. Foreign citizens/ entities are however not allowed to invest in mutual funds in India.

2.2.1.3 PRESENT POSITION OF MUTUAL FUNDS IN INDIA

Average Assets Under Management (AAUM) of Indian Mutual Fund Industry for the month of November 2017 stood at ₹ 22.73 lakh crore. Assets Under Management (AUM) as on November 30, 2017 stood at ₹ 22.79 lakh crore. The AUM of the Indian MF Industry has grown from ₹ 3.26 trillion as on 31st March 2007 to ₹ 22.79 trillion as on 30th November, 2017, about seven fold increase in a span of about 10 and half years. The MF Industry's AUM has grown from ₹5.87 trillion as on 31st March, 2012 to ₹ 22.79 trillion as on 30th November, 2017, about four fold increase in a span of about 5 and half years. The Industry's AUM had crossed the milestone of ₹10 Trillion (₹10 Lakh Crore) for the first time in May 2014 and in a short span of about three and half years, the AUM size has increased more than two folds and stood at ₹ 22.79 Trillion (₹ 22.79 Lakh Crore) as on 30th November, 2017.The total number of accounts (or folios as per mutual fund parlance) as on November 30, 2017 stood at 6.49 crore (64.9 million), while the number of folios under Equity, ELSS and Balanced schemes, wherein the maximum investment is from retail segment stood at 5.30 crore (53 million).

2.2.2 Part B: Portfolio Management: Meaning, Objectives, Importance, Issues in Portfolio Construction-Revision-Evaluation

2.2.2.1 INTRODUCTION OF PORTFOLIO:

"Portfolio means combined holding of many kinds of financial securities i.e. shares, debentures, government bonds, units and other financial assets." The term investment portfolio refers to the various assets of an investor which are to be considered as a unit. It is not merely a collection of unrelated assets but a carefully blended asset combination within a unified framework. It is necessary for investors to take all decisions as regards their wealth position in a context of portfolio. Making a portfolio means putting ones eggs in different baskets with varying element of risk and return. The object of portfolio is to reduce risk by diversification and maximise gains. Thus, portfolio is a combination of various instruments of investment. It is also a combination of securities with different risk-return characteristics. A portfolio is built up out of the wealth or income of the investor over a period of time with a view to manage the risk-return preferences. The analysis of risk-return characteristics of individual securities in the portfolio is made from time to time and changed that may take place in combination with other securities are adjusted accordingly. The object of portfolio is to reduce risk by diversification and maximize gains.

PORTFOLIO MANAGEMENT

Portfolio management means selection of securities and constant shifting of the portfolio in the light of varying attractiveness of the constituents of the portfolio. It is a choice of selecting and revising spectrum of securities to it in with the characteristics of an investor. Portfolio management includes portfolio planning, selection and construction, review and evaluation of securities. The skill in portfolio management lies in achieving a sound balance between the objectives of safety, liquidity and profitability. Timing is an important aspect of portfolio revision. Ideally, investors should sell at market tops and buy at market bottoms. Investors may switch from bonds to share in a bullish market and vice-versa in a bearish market. Portfolio management is all about strengths, weaknesses, opportunities and threats in the choice of debt vs. equity, domestic vs. international, growth vs. safety, and many other tradeoffs encountered in the attempt to maximize return at a given appetite for risk. Portfolio management is an art and science of making decisions about investment mix and policy, matching investments to objectives, asset allocation for individuals and institutions, and balancing risk against performance. Portfolio management in common parlance refers to the selection of securities and their continuous shifting in the portfolio to optimize the returns to suit the objectives of the investor. This however requires financial expertise in selecting the right mix of securities in changing market conditions to get the best out of the stock market. In India, as well as in many western countries, portfolio management service has assumed the role of specialized service now a days and a number of professional merchant bankers compete aggressively to provide the best to high net-worth clients, who have little time to manage their investments. The idea is catching up with the boom in the capital market and an increasing number of people are inclined to make the profits out of their hard earned savings. Markowitz analysed the implications of the fact that the investors, although seeking high expected returns, generally wish to avoid risk. It is the basis of all scientific portfolio management. Although the expected return on a portfolio is directly related to the expected returns on component securities, it is not possible to deduce a portfolio riskiness simply by knowing the riskiness of individual securities. The riskiness of portfolio depends upon the attributes of individual securities as well as the interrelationships among securities. A professional, who manages other people's or institution's investment portfolio with the object of profitability, growth and risk minimization is known as a portfolio manager. He is expected to manage the investor's assets prudently and choose particular investment avenues appropriate for particular times aiming at maximization of profit. Portfolio management includes portfolio planning, selection and construction, review and evaluation of securities. The skill in portfolio management lies in achieving a sound balance between the objectives of safety, liquidity and profitability. Timing is an important aspect of portfolio revision. Ideally, investors should sell at market tops and buy at market bottoms. They should be guarded against buying at high prices and selling at low prices. Timing is a crucial factor while switching between shares and bonds. Investors may switch from bonds to shares in a bullish market and vice-versa in a bearish market. Portfolio management service is one of the merchant banking activities recognized by Securities and Exchange Board of India (SEBI). The portfolio management service can be rendered either by the SEBI recognized categories I and II merchant bankers or portfolio managers or discretionary portfolio manager as defined in clause (e) and (f) of rule 2 SEBI (portfolio managers) Rules 1993. According to the definitions as contained in the above clauses, a portfolio manager means any person who pursuant to contract or arrangement with a client, advises or directs of undertakes on behalf of the client (whether as a discretionary portfolio manager or otherwise) the management or administration of a portfolio of securities or the funds of the client, as the case may be. A merchant banker acting as a portfolio Manager shall also be bound by the rules and regulations as applicable to the portfolio manager. Realizing the importance of portfolio management services, the SEBI has laid down certain guidelines for the proper and professional conduct of portfolio management services. As per guidelines only recognized merchant bankers registered with SEBI are authorized to offer these services. Portfolio management or investment helps investors in effective and efficient management of their investment to achieve their financial goals. The rapid growth of capital markets in India has opened up new investment avenues for investors. The stock markets have become attractive investment options for the common man. But investors should be able to effectively and efficiently manage investments in order to keep maximum returns with minimum risk. A portfolio manager by virtue of his knowledge, background and experience is expected to study the various avenues available for profitable investment and advise his client to enable the latter to maximize the return on his investment and at the same time safeguard the funds invested.

2.2.2.2 OBJECTIVES OF PORTFOLIO MANAGEMENT

1) Security/Safety of Principal: Security not only involves keeping the principal sum intact but also keeping intact its purchasing power intact. Safety means protection for investment against loss under reasonably variations. In order to provide safety, a careful review of economic and industry trends is necessary. In other words, errors in portfolio are unavoidable and it requires extensive diversification. Even investor wants that his basic amount of investment should remain safe.

2) Stability of Income: So as to facilitate planning more accurately and systematically the reinvestment consumption of income is important.

3) Capital Growth: This can be attained by reinvesting in growth securities or through purchase of growth securities. Capital appreciation has become an important investment principle. Investors seek growth stocks which provides a very large capital appreciation by way of rights, bonus and appreciation in the market price of a share.

4) Marketability: It is the case with which a security can be bought or sold. This is essential for providing flexibility to investment portfolio.

5) Liquidity i.e. nearness to money: It is desirable to investor so as to take advantage of attractive opportunities upcoming in the market.

6) Diversification: The basic objective of building a portfolio is to reduce risk of loss of capital and / or income by investing in various types of securities and over a wide range of industries. 7) Favorable Tax status (Tax Incentives): The effective yield an investor gets form his investment depends on tax to which it is subject. By minimizing the tax burden, yield can be effectively improved. Investors try to minimise their tax liabilities from the investments. The portfolio manager has to keep a list of such investment avenues along with the return risk, profile, tax implications, yields and other returns. Investment programmers without considering tax implications may be costly to the investor.

Portfolio Risk and Return

Every financial decision has two aspects these are risk and return as these are the two main determinants of security prices. They have their impact on the share prices as well as the valuation of firm. Every decision involves some degree of risk, so an investor has to take his financial decision rationally to optimize his returns through the calculations of risk and return.

Return is associated with gain or loss on money invested in the market. The rate of return on a security is the annual income received plus any change in the market price of an asset. Return is required to maximize the market price of the share but return is associated with risk because the greater the return, higher the expectation of risk. An investor has to consider the risk of different financing patterns to balance his decision between risk and return. Like the return is expected to be high for investing in purchase of an equity share in the market, but such a return is associated with high risk. Govt securities have a low risk as they provide stable return but at very low rate. Thus the investor has to pay the price in term of loss of return in order to invest in safe securities having minimum risk Since investment decision is based on future estimated returns which are exposed to different kinds of risk, so forecasts cannot be made with certainty. Thus Risk and returns are closely related.

A profitable investment may also be very risky. So an investor has to manage a trade off between risk and return.

The variability of the actual return from the expected returns associated with the given asset is defined as a risk. The greater variability is associated with the risky securities like equity shares and the more certainty of return is associated with the government securities like Treasury-Bills have lesser variability and thus are less risky. Risks on investment like bank deposit are considered to be quite safe, but rate of interest can change depending on the policy of RBI. Investments in equity securities of a firm possess higher degree of risk as compared to govt securities and bank deposits as they are surrounded by market risk, which is quite uncontrollable because they are broad spectrum depending on market forces.

An investor has to take a decision in investing the firm's funds in such a way to optimize return along with minimization of risk. This combination is called the risk return trade- off. This is the level where the market price of the share is maximized. The balance brought about by matching risk and return help in achieving the objectives of wealth maximization.

The investor tries to reduce risk by understanding the risk environment. Risk consists of two types of exposures i.e. systematic and unsystematic exposures.

Systematic risk- Systematic risk is due to the broad spectrum of uncontrollable risk associated with the business activities within a country. It generates out of macroeconomic environmental factors such as demand, supply, inflation, change in interest rates, and change in government policies backed by sociological and political factors in a country. It is an uncontrollable risk as these forces are beyond the control of any individual and thus cannot be minimized by a single firm. They have their strong influence on the market conditions. Such risks are called market risk and interest risk and purchasing power risk. These risks affect the cash inflows of a project. The changes in cash inflows will also bring about change in the profitability of an investment proposal.

Unsystematic risk- Unsystematic risk is a unique risk related to the company pertaining to the behaviour pattern or internal influence of a firm like the problems relating to management, staff, expenses, losses, strikes and other issues directly affect the company's own operations. These are controllable risks and thus can be minimized by diversification of investment portfolio.

Thus an investor must analyse the existence of the degree of above mentioned two risks to balance his decision of risk and return to get potential gains at minimum risk

Return measurement- Securities provide returns in the form of dividends or interests and it also provides a return at the time of sale in the form of capital gain. These securities have to be valued at different points of time. The returns at a particular point of time are required to be calculated by discounting the returns at an appropriate discount rate, which depends upon the individual's own perception of risk. The discount rate which is also called the required rate of return show the risk of the cash flows. It would also help to determine the value of the asset. The higher the discount rate greater will be the risk level. Thus the value of an asset therefore varies according to the risk perception and estimation of each individual. The required rate of return can be calculated with the help of the following formula-

K= If+Rp

Where

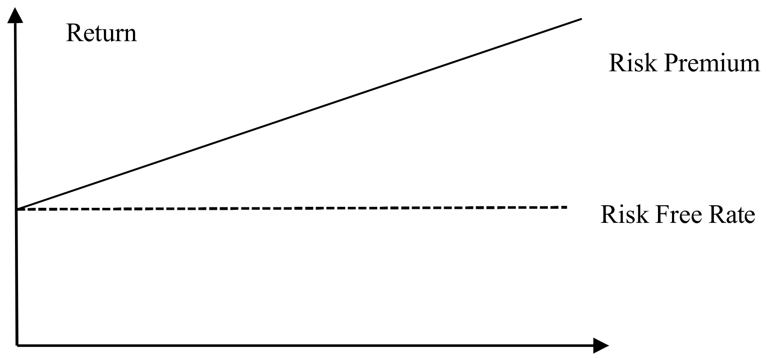
K= required rate of return

If= risk free rate

Rp= Risk premium

The risk free rate remains the same irrespective of any increase or decrease of risk level. The risk premium which indicates the compensation for taking the risk increases with increase in risk and decreases with decreasing risk. Thus the required rate of return comprises of the risk free rate, the risk perception and risk premium.

Figure 1 : Chart showing risk and return



In the above figure the X-axis shows level of risk and Y-axis depicts the rate of return. From the point of origin and up to If is the risk free zone. The slope after the risk free rate slopes upward as this is the risk premium for compensating high risk with higher return. **Risk Measurement**- The risk associated with a security from both a behavioural and a quantitative/statistical point of view. Different techniques are available to measure these different risks. The behavioural view of risk can be measured by using sensitivity analysis and probability distribution. The statistical measures of risk of a security are standard deviation and coefficient of risk.

a. Sensitivity Analysis- It is a behavorioul approach to assess risk by taking into account a number of possible return estimates so that a sense of variability among outcomes can be measured. In order to have a sense of variability among return estimates, a possible approach is to estimate the worst (pessimistic), the expected (most likely) and the best (optimistic) return associated with the asset. The difference between the optimistic and pessimistic outcomes is the range which according to sensitivity analysis is the basic measure of risk. The greater range indicates the more variability of the asset.

Probability distribution- The risk associated with an asset can be assessed more accurately by the use of probability distribution than sensitivity analysis. It is a model that relates probabilities to the associated outcomes. The probability of an outcome represents the likelihood/percentage chance of its occurrence. For example if the expectation is that a given outcome will occur eight out of ten times, it can be said to have eighty percent chance of occurrence. If it is certain to happen, the probability of happening is 100 percent. An outcome which has a probability of zero indicates that this outcome will never occur. Based on the probabilities assigned to the rate of return, the expected value of the return can be computed which is the weighted average of all possible returns multiplied by their respective probabilities. Thus, probabilities of the various outcomes are used as weights. The expected return,

Re=∑sum of Ri*Pri Where

Re= Expected Return

Ri= Return for the i^{th} possible outcome Pri=probability associated with its return

N=number of outcomes considered

a. **Standard deviation of return**- Risk refers to the dispersion of returns around an expected value. The most common statistical measure of risk of an asset is the standard deviation from the mean /expected value of return. It represents the square root of the average squared deviations of the individual returns from the expected returns, symbolically the standard deviation

$$\sigma = \sqrt{\sum_{i=1}^{n} (Ri - Re)^2 * Pr_i}$$

where

σ = Standard Deviation of Returns

Re= Expected Return

Ri= Return for the i^{th} possible outcome

ri=probability associated with its return

N=number of outcomes considered.

The greater standard deviation of returns indicates the greater variability/dispersion of returns and the greater risk of the investment. It is the absolute measure of dispersion and does not consider the variability of return in relation to the expected value.

Coefficient of variation- It is a measure of relative dispersion used in comparing the risk of assets with differing expected returns. It is a measure of risk per unit of expected return. It converts standard deviation of expected values into relative values to enable comparison of risks associated with assets having different expected values. The coefficient of variation is computed by dividing the standard deviation for an asset by its expected value.

CV= σr/Re Where

CV= Coefficient ofvariation

σr= Standard deviation of return

Re = Expected Return

The larger CV is associated with the larger relative risk of the asset. The use of coefficient of variation for comparing asset risk is the best since it considers the relative size (expected value) of assets.

The capital asset pricing model is an equilibrium model of the trade off between expected security return and systematic risk which is unavoidable. It is the basic theory that links together risk and return of all assets and also explains how the security prices are calculated in the market place.

It provides the framework for determining the equilibrium expected return for risky securities by deriving the relationship between expected return and systematic risk of individual securities and portfolios. Thus the CAPM has implications for

- Risk returns relationship for an efficient portfolio as well as for an individual security.
- Identification of under and over-valued assets traded in the market.
- Pricing of asset not yet traded in the market.
- Effect of leverage on cost of equity (rate of return required by equity shareholders)
- Capital budgeting decisions and cost of capital.
- Risk of firm through diversification of project portfolio.

Assumptions

- The CAPM makes certain simplifying assumptions to remove the complexities of the model. Some of them may be relaxed later:
- All investors are price takers. They are large in number so that no single investor can affect prices.
- All investors use the mean- variance portfolio selection model of Markowitz's asset pricing model.
- Assets/securities are perfectly divisible.
- All investors plan for one identical holding period.

Investors can lend or borrow at an identical risk-free rate.

- There are no transaction costs and income taxes.
- The market price of share is influenced by systematic and unsystematic risk. The

CAPM approach measures the systematic risk of the security. Such a risk is measured by beta which measures change in market value of equity shares relative to change in market index. If beta is high the company's share will have high risk. The CAPM model calculates cost of equity through the following equation:

- $Ke = Kf + \beta(Km - Kf)$
- Ke = cost of equity capital

  Kf = cost of risk free asset
- β = coefficient of systematic risk
- Km = cost of market portfolio

In the CAPM, the expected return on an asset varies directly with its systematic risk and the risk premium of market portfolio which is a reward depending on the level of risk free return and return on the market portfolio. In other words, the risk premium for an asset or portfolio is a function of its beta i.e. the risk premium added to the risk free rate is directly proportion to beta

Thus the three basic elements required to apply CAPM model are: risk free rate, risk premium on market portfolio and beta.

Risk free rate- The rate of return available on an assets like T- bills, money market funds or bank deposits is taken as the proxy for risk free rate as such assets have very low or virtually negligible default risk and interest rate risk. However under inflationary conditions, they are risk less in nominal terms only. In fact, real return (nominal return- inflation rate) may become zero, even negative when inflation wakes up.

Risk premium on market portfolio- The risk premium on market portfolio is the difference between the expected return on the market portfolio and the risk free rate of the return. The CAPM holds that in equilibrium the market portfolio is the unanimously desirable risky portfolio. It contains all securities in proportion to their market value. In the efficient portfolio, which enables neither lending and borrowing, the risk premium on the market portfolio is proportional to its risk and the degree of risk aversion of the average investor.

Beta- Beta measures the risk (Volatility) of an individual security relative to market portfolio. Accordingly, beta is the co variance of the security's return with the market portfolio's return, divided by the variance of market portfolio. The co-variance of two securities is the product of their correlation coefficient and respected standard deviation. The covariance of the market portfolio with itself is the variance of the portfolio. Thus the beta of the market portfolio is one. This classifies all other market portfolios and securities in the two risky classes. Securities with beta less than one are called defensive security. Security with beta greater than one is called aggressive security. Risk free security has a beta equal to zero.

Portfolio revision

Portfolio Revision The process of addition of more assets in an existing portfolio or changing the ratio of funds invested is called as portfolio revision. The sale and purchase of assets in an existing portfolio over a certain period of time to maximize returns and minimize risk is called as Portfolio revision. There are two types of Portfolio Revision Strategies. • Active Revision Strategy Active Revision Strategy involves frequent changes in an existing portfolio over a certain period of time for maximum returns and minimum risks. Active Revision Strategy helps a portfolio manager to sell and purchase securities on a regular basis for portfolio revision. • Passive Revision Strategy Passive Revision Strategy involves rare changes in portfolio only under certain predetermined rules. These predefined rules are known as formula plans. According to passive revision strategy a portfolio manager can bring changes in the portfolio as per the formula plans only. Portfolio Evaluation Portfolio evaluating refers to the evaluation of the performance of the investment portfolio. It is essentially the process of comparing the return earned on a portfolio with the return earned on one or more other portfolio or on a benchmark portfolio. The evaluation of the portfolio provides a feed back about the performance to evolve better management strategy. Evaluation of portfolio performance is considered to be the last stage of investment process. Sharpe ind index measures the risk premium of the portfolio relative to the total amount of risk in the portfolio. • Sharpe Index • Treynor's Performance Index • Jensen's Performance Index

The absolute risk adjusted return measure was developed by Michael Jensen. The standard is based on the manager's predictive ability. The basic model of Jensen is: $Rp = a + b\ (Rm - Rf)$ Steps in Investment Process When investing for lifelong goals, the portfolio planning process never stops. As investors move through their life stages, changes may occur, such as job changes, births, divorce, deaths, or shrinking time horizons, which may require adjustments to their goals, risk-reward profiles or asset allocations. As changes occur, or as market or economic conditions dictate, the portfolio planning process begins anew, following each of the five steps to ensure that the right investment strategy is in place. Investment is a process of acquiring an asset with an aim to generate money from it. Generating income from an asset can be through regular income or appreciation of the asset.

PORTFOLIO MANAGEMENT PROCESS

Portfolio management is on-going process involving the following basic tasks: i. Identification of the investor's objectives, constraints and preferences. ii. Strategies are to be developed and implemented in tune with investment policy formulated. iii. Review and monitoring of the performance of the portfolio. iv. Finally the evaluation of the portfolio and make some adjustments for the future.

CONSTRUCTION OF PORTFOLIO:

Portfolio construction means determining the actual composition of portfolio. It refers to the allocation of funds among a variety of financial assets open for investment. Portfolio theory concerns itself with the principles governing such allocation. Therefore, the objective of the theory is to elaborate the principles in which the risk can be minimized subject to a desired level of return on the portfolio or maximize the return subject to the constraints of a certain level of risk. The portfolio manager has to set out all the alternative investments along with their projected return and risk, and choose investments which satisfy the requirements of the investor and cater to his preferences. It is a critical stage because asset mix is the single most determinant of portfolio performance. Portfolio construction requires a knowledge of the different aspects of securities. The components of portfolio construction are (a) Asset allocation (b) Security selection and (c) Portfolio structure. Asset allocation means setting the asset mix. Security selection involves choosing the appropriate security to meet the portfolio targets and portfolio structure involves setting the amount of each security to be included in the portfolio. Investing in securities presupposes risk. A common way of reducing risk is to follow the principle of diversification. Diversification is investing in a number of different securities rather than concentrating in one or two securities. The diversification assures the benefit of obtaining the anticipated return on the portfolio of securities. In a diversified portfolio, some securities may not perform as expected but other securities may exceed expectations with the effect that the actual results of the portfolio will be reasonably close to the anticipated results.

MEARCHANT BANKING / INVESTMENT BANKING

A merchant bank is a financial institution primarily engaged in offering financial services and advice to corporations and to wealthy individuals. The term can also be used to describe the private equity activities of banking. The chief distinction between an investment bank and a merchant bank is that a merchant bank invests its own capital in a client company whereas an investment bank purely distributes (and trades) the securities of that company in its capital raising role. Both merchant banks and investment banks provide fee based corporate advisory services. Merchant banking services are provided by the financial institutions, subsidiaries of many commercial banks and by the private sector. The activities that merchant bankers are authorised to perform are listed by the SEBI and include issue management, loan syndication, lease financing, corporate advisory services, underwriting, portfolio management services and managers or consultants to public issues.

ROLE OF PORTFOLIO MANAGER

A portfolio manager is a person who makes investment decisions using money other people have placed under his or her control. In other words, it is a financial career involved in investment management. They work with a team of analysts and researchers, and are ultimately responsible for establishing an investment strategy, selecting appropriate investments and allocating each investment properly for a fund- or asset-management vehicle. Portfolio managers are presented with investment ideas from internal buyside analysts and sell-side analysts from investment banks. It is their job to sift through the relevant information and use their judgment to buy and sell securities. Throughout each day, they read reports, talk to company managers and monitor industry and economic trends looking for the right company and time to invest the portfolio's capital. A team of analysts and researchers are ultimately responsible for establishing an investment strategy, selecting appropriate investments and allocating each investment properly for a fund or asset-management vehicle. Portfolio managers make decisions about investment mix and policy, matching investments to objectives, asset allocation for individuals and institutions, and balancing risk against performance. A professional, who manages other people's or institution's investment portfolio with the object of profitability, growth and risk minimization, is known as a portfolio manager. They are expected to manage the investor's assets prudently and choose particular investment avenues appropriate for particular times aiming at maximization of profit. The role of portfolio manager includes the following,

1. Quantify their clients’ risk tolerances and return needs by taking into account his liquidity, income, time horizon, expectations
2. Do an optimal asset allocation and choose strategy that meets the clients needs
3. Diversify the portfolio to eliminate the unsystematic risk
4. Monitor the changing market scenario, expectations, client needs etc and rebalance accordingly
5. Lower the transaction cost by minimizing the taxes, trading turnover, and liquidity costs.

COLLECTING THE BASIC DATA :

Initially, the portfolio manager has to devote a great deal of attention to basic consideration such as pension plans, life insurance and educational funds for children. Usually, the basic needs must be satisfied before making an investment programme. Every individual investor has a priority of expenditures. The following list of priority expenditure is probably representative. a) Food, clothing, housing and transportation. b) Life insurance. c) Pension plan. d) Savings for emergency. e) Investments. Investments in securities can be considered only after basic family needs are satisfied. The type of data that can be collected about the investor includes the following items: a) Stated purpose for the portfolio, b) Age and health of the family. c) Marital status and responsibilities. d) Occupation. e) Approximate income, sources and expected duration. f) Saving habits. g) Property ownership. h) Current security holdings. . If all priority expenditures have been satisfied, the portfolio manager has greater freedom to pursue a more aggressive policy.

FORMULATING THE PORTFOLIO OBJECTIVES

The portfolio objectives can be determined by ascertaining the constraints on portfolio. The greater the number of constraints and the more binding these constraints, more conservative the portfolio must be. The following are the six possible portfolio constraints which are evaluated to determine the appropriate objectives:

1. Need for current income to meet the living expenses.
2. Need for constant income to face inflation.
3. Need for safety principal to liquidate the investments on a short notice.
4. Need for safety principal to reduce the effect of purchasing power.
5. Need for tax exemption.
6. Temperament

2.2.2.3 NEED FOR DESIGNING AN INVESTMENT PORTFOLIO

There are large numbers of savers in India. It is also surprising that the saving rate in India is as high as 32% of GDP per annum and investment at 34% of GDP. High levels of investment could not generate comparable rates of growth of output because of poor investment strategy, high capital output ratios, low productivity of capital and high rates of obsolescence of capital. Thus, the use of capital in India is wasteful and inefficient. The portfolio managers lack the expertise and experience. The average Indian household saves around 55% in financial form and 45% in physical form. As per latest RBI data, savings in the financial form is held 64% in cash and bank deposits which gives negative real returns. Around 24% of financial savings is held in the form of Insurance, Provident Fund, Pension Funds and 5% is in Government Securities like post office savings, NSCs, Public Provident Funds, National Savings Schemes etc. The investment in capital market instruments is around 6% of the total financial savings. Their objectives are capital appreciation, safety marketability, liquidity and hedge against inflation. The investors should follow proper strategy for investment management. Therefore, portfolio management becomes desirable. Indian markets are developing and all the basic principles and theories of portfolio management would apply in the market. Since 1952, investors have better understood the dimension of attractiveness and why the rational and professional management of portfolios includes more than the listing of securities by the magnitude of their expected returns. The great 1952 event was the publication of Harry Markowitz's celebrated article "Portfolio selection." Markowitz analyzed the implications of the fact that investors although seeking high expected returns generally wish to avoid risk. Since there is overwhelming evidence that risk aversion characterizes most investors, especially most large-investor's rationality in portfolio management demands that account be taken not only expected returns for a portfolio but also of the risk that is incurred. Although the expected return on a portfolio is directly related to the expected returns on component securities, it is impossible to deduce a portfolio's riskiness simply by knowing the riskiness of individual securities. The riskiness of portfolios depends not only on the attributes of individual securities, but also on the interrelationships among securities. Therefore, it is primarily for this reason that portfolio management is desirable. Another reason for the need for portfolio management is that it depends upon the preferences of individual investors. It is possible to estimate expected returns for individual securities without regard to any investor, but it is impossible to construct on optimal portfolio for an investor without taking personal preferences into account. The output of security analysts is essential for portfolio management or at least portfolio managers make use of security analysts output but this output must be analyzed with reference to the tastes and financial circumstances of individual investors when building portfolios. Portfolio management is still in its infancy in India. Professional portfolio management started in India after the setting up of public sector mutual funds in 1987. After the success of mutual funds in portfolio management, a number of brokers and investment consultants have become portfolio managers. Basically portfolio management is required for proper investment decision-making regarding buy and sell of securities. There is a need for proper money management in terms of investment as a basket of assets so as to satisfy the asset preferences of the investors and to reduce the risk and increase the returns on investment.

POPULARITY OF EQUITY PORTFOLIO MANAGEMENT SERVICES

Portfolio Management Service (PMS) is a professional service rendered for management of portfolio of others with the help of experts in Investment advisory services. It involves continuing relationship with client to manage investments with or without discretion for the client as per his requirements. Portfolio management is an art and requires high degree of expertise. The SEBI has set out guidelines in which the relationship of the client and the portfolio manager and the respective rights and duties of both have been set out. The job of the portfolio manager in managing the client's fund either on discretionary or non-discretionary basis has become challenging and difficult due to the multitude of obligations laid on his shoulders by the SEBI, in respect of their operations, accounts and audit. Thus, portfolio management has become a complex and responsible job which requires an in-depth training and expertise. The activities of buying and selling of securities in the primary as well as secondary market are carried out through the mechanism of stock exchanges. There has been a substantial growth of capital market in India during the last 25 years. There are 23 stock exchanges in India and more than 9500 listed companies. There were 56,588 capital issues and the market value of capital was Rs.12,01,207 crores till 2004-05. As per SEBI regulations, only those who are registered with SEBI are eligible to operate as a portfolio manager. They have to pay required license fees. For this purpose the eligible persons should have necessary infrastructure with professionally qualified persons and minimum net worth of Rs.50 lakhs. The SEBI has imposed a number of obligations and a code of conduct on the portfolio managers.

TYPES OF PORTFOLIO

When it comes to investing there are many options available to individuals. A person can invest in stocks, bonds, mutual funds, etc. Once a person invests in multiple products their performance needs to be tracked and strategies made to ensure the investor reaps the most profit possible. This is where the investment portfolio comes into play. According to Investor Awareness, it is a term that describes all investments owned. To take this definition a little farther, an investment portfolio is a significant aspect in diversification. Maintaining a diverse portfolio helps to mitigate loss because the investor has not placed all of their eggs in one basket. There are different types of investment portfolios. Perhaps the most common type's individuals are exposed to are: Conservative, Balanced and Aggressive Growth. A portfolio is a combination of different investment assets mixed and matched for the purpose of achieving an investor's goals. Items that are considered a part of Investors portfolio can include any asset that they own - from real items such as art and real estate, to equities, fixed-income instruments and their cash and equivalents. For the purpose of this section, Investors will focus on the most liquid asset types: equities, fixed-income securities and cash and equivalents. The asset mix they choose according to their aims and strategy will determine the risk and expected return of their portfolio. 1. Aggressive Investment Portfolio In general, aggressive investment strategies - those that shoot for the highest possible return - are most appropriate for investors who, for the sake of this potential high return, have a high risk tolerance and a longer time horizon. Aggressive portfolios generally have a higher investment in equities. Aggressive investment portfolios are for investors not afraid of high risk. This type of portfolio may incorporate mutual funds that aim for high capital gain, equities, stocks, bonds, cash and maybe some commodities. In the short-term, growth will be very small and some loss will be observed. As a result, aggressive portfolios perform better in the long term - about five years or longer. An actively traded aggressive portfolio will typically gain maximum returns for the investor. The loss factor is why only individuals who are willing to take a high financial risk should seek an aggressive investment portfolio. An aggressive portfolio contains high growth investments that will hopefully appreciate in value. This strategy attempts to achieve high long-term growth by investing in often risky but profitable, short-term stocks. Under normal market conditions, the Aggressive Growth Portfolio will invest approximately 100% of its total assets in equity securities. The Aggressive Growth Portfolio can invest up to 100% of its total assets in equity securities and up to 25% of its total assets in fixed income securities. 2. Balanced or Moderate Investment Portfolio A moderately aggressive portfolio is meant for individuals with a longer time horizon and an average risk tolerance. Investors who find these types of portfolios attractive are seeking to balance the amount of risk and return contained within the fund. The portfolio would consist of approximately 50-55% equities, 35-40% bonds, 5-10% cash and equivalents. The Moderate Portfolio's primary investment objective is to seek long-term capital appreciation and also the Moderate Portfolio seeks current income. 3. Conservative Investment Portfolio The conservative investment strategies, which put safety at a high priority, are most appropriate for investors who are risk averse and have a shorter time horizon. Conservative portfolios will generally consist mainly of cash and cash equivalents, or high-quality fixed-income instruments. The main goal of a conservative portfolio strategy is to maintain the real value of the portfolio, or to protect the value of the portfolio against inflation. The portfolio shown below would yield a high amount of current income from the bonds and would also yield long-term capital growth potential from the investment in high quality equities. The conservative investment portfolio is geared towards preserving capital. A minimal risk investment strategy is used. This type of portfolio is ideal for retirees who are focused more on having assets available than a stream of income from interest. Since the primary goal is to preserve capital, investors can dip into their principal to supplement living expenses instead of relying on the portfolio's earned income. The Conservative Portfolio's primary investment objective is to seek preservation of capital and current income. The Conservative Portfolio also seeks capital appreciation. Under normal market conditions, the Conservative Portfolio will invest approximately 65% of its total assets in fixed income securities and cash and approximately 35% of its total assets in equity securities. The Conservative Portfolio can invest up to 100% of its total assets in fixed income securities and or some time up to 20% of its total assets in equity securities. Investors can further break down the above asset classes into subclasses, which also have different risks and potential returns. For example, an investor might divide the equity portion between large companies, small companies and international firms. The bond portion might be allocated between those that are short-term and long-term, government versus corporate debt, and so forth. More advanced investors might also have some of the alternative assets such as options and futures in the mix. As, the number of possible asset allocations is practically unlimited.

NEED AND IMPORTANCE OF PORTFOLIO MANAGEMENT

Portfolio management is a process encompassing many activities of investment in assets and securities. It is a dynamic and flexible concept and involves regular and systematic analysis, judgment and action. The objective of this service is to help the unknown and investors with the expertise of professionals in investment portfolio management. It involves construction of a portfolio based upon the investor's objectives, constraints, preferences for risk and returns and tax liability. The portfolio is reviewed and adjusted from time to time in tune with the market conditions. The evaluation of portfolio is to be done in terms of targets set for risk and returns. The changes in the portfolio are to be effected to meet the changing condition. Portfolio construction refers to the allocation of surplus funds in hand among a variety of financial assets open for investment. Portfolio theory concerns itself with the principles governing such allocation. The modern view of investment is oriented more go towards the assembly of proper combination of individual securities to form investment portfolio. A combination of securities held together will give a beneficial result if they grouped in a manner to secure higher returns after taking into consideration the risk elements. The modern theory is the view that by diversification risk can be reduced. Diversification can be made by the investor either by having a large number of shares of companies in different regions, in different industries or those producing different types of product lines. Modern theory believes in the perspective of combination of securities under constraints of risk and returns.

2.2.3 Part C: Financial Inclusion: Meaning, Need, Government Policy

2.2.3.1 Introduction :

With the progress of the Indian economy, especially when the focus is on the achievement of sustainable development, there must be an attempt to include maximum number of participation from all the sections of the society. But the lack of awareness and financial literacy among the rural population of the country is hindering the growth of the economy as majority of the population does not have access to formal credit. This is a serious issue for the economic progress of the country. In order to overcome such barriers, the banking sector emerged with some technological innovations such as automated teller machines (ATM), credit and debit cards, internet banking, etc. Though introduction of such banking technologies brought a change in the urban society, a majority of the rural population is still unaware of these changes and is excluded from formal banking. Financial inclusion enables improved and better sustainable economic and social development of the country. It helps in the empowerment of the underprivileged, poor and women of the society with the mission of making them self-sufficient and well informed to take better financial decisions. Financial inclusion takes into account the participation of vulnerable groups such as weaker sections of the society and low income groups, based on the extent of their access to financial services such as savings and payment account, credit insurance, pensions etc. Also the objective of financial inclusion exercise is easy availability of financial services which allows maximum investment in business opportunities, education, save for retirement, insurance against risks, etc. by the rural individuals and firms. The penetration of financial services in the rural areas of India is still very low. The factors responsible for this condition can be looked at from both supply side and demand side and the major reason for low penetration of financial services is, probably, lack of supply. The reasons for low demand for financial services could be low income level, lack of financial literacy, other bank accounts in the family, etc. On the other hand, the supply side factors include no bank branch in the vicinity, lack of suitable products meeting the needs of the poor people, complex processes and language barriers. Since 2005, the Reserve Bank of India (RBI) and the Government of India (GOI) have been making efforts to increase financial inclusion. Measures such as SHG-bank linkage program, use of business facilitators and correspondents, easing of Know Your Customer (KYC) norms, electronic benefit transfer, separate plan for urban financial inclusion, use of mobile technology, bank branches and ATMs, opening and encouraging 'no-frill-accounts' and emphasis on financial literacy have played a significant role for increasing the use of formal sources for availing loan/ credit. Measures initiated by the government include, opening customer service centers, credit counselling centers, Kisan Credit Card, Mahatma Gandhi National Rural Employment Guarantee Scheme and Aadhar Scheme. These renewed efforts are more focused than the earlier measures which were more general in nature having a much wider scope. Though the measures were initiated earlier, their impact on the rural population needs to be analysed and reframed in order to understand the present scenario in the rural areas. This paper is arranged in six sections.

Definition of Financial Inclusion:

According to the Planning Commission (2009), Financial inclusion refers to universal access to a wide range of financial services at a reasonable cost. These include not only banking products but also other financial services such as insurance and equity products. The household access to financial services includes access to contingency planning, credit and wealth creation. Access to contingency planning would help for future savings such as retirement savings, buffer savings and insurable contingencies and access to credit includes emergency loans, housing loans and consumption loans. On the other hand, access to wealth creation includes savings and investment based on household's level of financial literacy and risk perception.

GOI (2008) defines Financial inclusion as the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost. The meaning of financial inclusion is delivery of financial services to the low income groups especially the excluded sections of the population with the provision of equal opportunities. The main target is the access of financial services for better standard of living and income.

According to Chakraborty (2011), Financial inclusion is the process of ensuring access to appropriate financial products and services needed by all sections of society including vulnerable groups such as weaker sections and low income groups at an affordable cost in a fair and transparent manner by mainstream institutional players. This issue started gaining importance recently in the news media. However, as is the case with several issues in India, financial inclusion has remained a pipe dream with a majority of Indians continuing to lack access to banking services.

Dimensions of Financial Inclusion The level of financial inclusion in India can be measured based on three tangible and critical dimensions. These dimensions can be broadly discussed under the following heads:

I. Branch Penetration Penetration of a bank branch is measured as number of bank branches per one lakh population. This refers to the penetration of commercial bank branches and ATMs for the provision of maximum formal financial services to the rural population.

II. Credit Penetration Credit Penetration takes the average of the three measures: number of loan accounts per one lakh population, number of small borrower loan accounts per one lakh population and number of agriculture advances per one lakh population.

III. Deposit Penetration Deposit penetration can be measured as the number of saving deposit accounts per one lakh population. With the help of this measure, the extent of the usage of formal credit system can be analysed. Among the three dimensions of financial inclusion, credit penetration is the key problem in the country as the all India average ranks the lowest for credit penetration compared to the other two dimensions. Such low penetration of credit is the result of lack of access to credit among the rural households. Therefore, the problem of low penetration needs to be understood more deeply. An attempt has been made to study the problem by examining the progress of financial inclusion over the years and efforts made by the government for reducing the low penetration of credit. The progress in the development of financial inclusion in India can be examined by understanding the stages involved in it. The concept of examining financial access became important immediately after the All-India Rural Credit Survey that was completed in the 1950s. The results of the survey revealed that farmers relied heavily on money-lenders in the year 1951-52. Only the urban areas had large number of bank branches compared to rural areas. Such a condition continued in the country until RBI started financial inclusion growth model in the 2000s. Because the urban areas were fully concentrated with numerous bank branches, this resulted in the higher absorption of bank credit in the urban areas. Thus, the growth of the private business credit was seen in the year 1957-61 from 44 percent to 60 percent in the year 19702.

2.2.3.2 Policy Initiatives for Financial Inclusion

For increasing the level of financial inclusion, the GOI and RBI have taken few actions which include the following:

- Nationalization of banks (1969, 1980)
- Priority Sector Lending requirements
- Establishment of Regional Rural Banks (RRBs) (1975, 1976)
- Service area approach (1989)
- Self-help group-bank linkage program (1989,1990)

The other measures taken by GOI, RBI and National Bank for Agriculture and Rural Development (NABARD) are :. Customer Service Centres, Credit Counselling Centres,Adhaar Scheme The National Agricultural Insurance Scheme, No-frill Account, Know Your Customer, General Credit Card Project on Processor Cards, Micro Finance Development Fund, Financial Inclusion Fund Project on “e-Grama” SHG-Post Office Linkage Financial Inclusion Technology Fund Separate Plan for Urban Financial Inclusion and Electronic Benefit Transfer Scheme Financial Literacy through Audio Visual medium - Doordarshan Support to Cooperative Banks and RRBs for setting up of Financial Literacy Centres Farmers’ Club Program Rural Volunteers etc. Though a number of measures have been initiated by the GOI, RBI and NABARD, the status of financial inclusion in the country still needs more support. The condition of financial inclusion in the different states of India in 2002 was not encouraging It shows that the all India percentage of the level of non-indebtedness, i.e. level of not accessing formal credit, of the rural household is 51.4 percent. This low credit penetration after years of measures was a matter of concern and still there is a lot of work to be done in the area of financial inclusion.

Need for Financial Inclusion:

Financial inclusion improves the country's financial system on a large scale. It improves the accessibility of economic resources. Most importantly, it reinforces the concept of saving among poor people in both urban and rural areas. In this way, it consistently contributes to the advancement of the economy.

Due to their vulnerable state, many poor people are exploited by rich landlords and unlicensed moneylenders. This serious and dangerous situation can be changed with the help of financial inclusion.

Financial inclusion entails bringing poor people into the formal banking system in order to secure their meager finances for the future. Many households have farmers or artisans who do not have adequate facilities to save the money they earn after putting in so much effort. Following are some of the important financial inclusion schemes in India:

Pradhan Mantri Jan Dhan Yojana (PMJDY)

The purpose behind this scheme is to expand affordable access such as Bank Accounts, Credits, Insurance and pension. Pradhan Mantri Jan Dhan Yojana was launched on 28th of August 2014. This scheme comes under the ministry of finance of India. On inauguration day itself i.e., on 28th of August 2014, 15 million bank accounts were opened on the very first day and by the end of the first week of this scheme, there were 18 million accounts were opened. In the next 4 years, 318 million bank accounts were opened and over 792 billion rupees were deposited under Pradhan Mantri Jan Dhan Yojana scheme. The main purpose of this scheme is that unbanked people should get a chance to open a bank account freely and become financially independent.

Pradhan Mantri MUDRA Yojana

The Government of India launched a flagship scheme called Prime Minister Mudra Yojana (PMMY) on 8th April 2015 in order to boost the economy. This scheme helps in getting affordable loans to the non-corporate, non-farm micro and small enterprises to fund their needs. Another goal of this scheme is to bring the target audience into the recognised financial fold, i.e., Financial Inclusion. MUDRA (Micro Units Development and Refinance Agency Limited) is a refinancing group providing loans up to Rs ten lakhs to the eligible enterprises at lower interest rates. This has been achieved through the Commercial Banks, RRBS, Cooperative Banks, NBFC and MFI. To access the loans, the borrowers need to approach the nearby branches of all the participating lending institutions and apply for loans under the MUDRA scheme. This scheme can also be availed online.

PM Jeevan Jyoti Bima Yojana

Life Insurance is a way to ensure that the family members of the deceased, don't have to face financial troubles paying for the daily expenses, housing payments or other loans or mortgages. Life Insurance continues to provide cover even after one has retired and the retiree is not getting any insurance from the erstwhile employer.

Pradhan Mantri Jeevan Jyoti Bima Yojana is one such kind of insurance scheme that offers insurance for a year, subject to the mandatory renewal on an annual basis, providing coverage for death. Launched on 9th May, the scheme was availed by more than5 crore people.

PM Suraksha Bima Yojana (PMSBY)

Pradhan Mantri Suraksha Bima Yojanais a Government scheme launched on 9th May 2015. It is a scheme introduced for accidental death proposed by finance minister during the budget speech in February 2015. Pradhan Mantri Suraksha Bima Yojana (PMSBY) gives an insurance policy and financial aid to the people belonging to the lower section of the society in case of any mishap or accident. All the Insurance companies from both the Private and Public sectors control this scheme.

Atal Pension Yojana (APY)

Atal Pension Yojana is a government-initiated pension scheme for workers employed in the unorganized sector in India. The Atal Pension scheme is an attempt to provide old-age security to the blue-collar workers like street vendors, rickshaw pullers, rag pickers, cobblers, workers in the agricultural sector and construction, landless labourers etc. Launched on 9th May 2015, the scheme replaces a government-run previous scheme named "Swavalamban Yojana" and is implemented and controlled by the Pension Fund Regulatory and Development Authority through NPS (National Pension System).

The Atal Pension scheme has been well-received by the people, garnering more than two and a half crore subscribers. Under the scheme, the government also offers a contributory amount of 50% of the total funds deposited by a worker.

Stand Up India Scheme

The Stand-Up India scheme aims to provide bank loans ranging from 10 lakh to 1 Crore to at least one Scheduled Caste (SC) or Scheduled Tribe (ST) borrower and at least one woman borrower per bank branch for the establishment of a greenfield enterprise.

This business could be in manufacturing, services, agriculture-related activities, or trading. In the case of non-individual enterprises, at least 51 percent of the shareholding and controlling stake must be held by a SC/ST or female entrepreneur.

Pradhan Mantri Vaya Vandana Yojana (PMVVY)

Pradhan Mantri Vaya Vandana Yojana is a pension scheme for elderly citizens above the age of 60 years or above, which provides a guaranteed pension for a span of 10 years. Due to the unstable market conditions and a matter of social security, a simplified scheme of assured pension of 8% was launched, which has been implemented through Life Insurance Corporation (LIC) of India. An investor is at the liberty of opting for the pension amount he/she wants or for the purchase price one wants to invest in. Launched in 2017 by the Ministry of Finance, the scheme was opened for enrolment till 31st March 2020. The scheme was given the nod again by the Finance Ministry and remained in effect till March 2023.

Varishtha Pension Bima Yojana (VPBY)

Varishtha Pension Bima Yojana is a senior citizen pension scheme initiated by the Government of India with administrative assistance from Life Insurance Corporation of India (LIC). Under this scheme, the subscribers receive annuity pay-outs until the maturity of the pension plan. VPBY was first announced in 2003-04 and later revived again in 2014-15, followed by 2017. The much-needed social security for senior citizens is promised with this scheme that ensures pension at 9% rate per year for 10 years with the period of pension return ranging from monthly to yearly. People above 60 years of age can subscribe to the plan. In the first phase of its launch, VPBY sold over 3 lakhs of policies with more than six thousand crores accumulated in the Government exchequer.

Sukanya Samriddhi Yojana

Sukanya Samriddhi Yojana was launched on 22nd January 2015 as a part of the Beti Bachao Beti Padhao campaign, with the primary goal of securing the future of a girl child. The Sukanya Samriddhi Yojana scheme aims to improve the lives of girls in the country. The Sukanya Samriddhi scheme was launched to provide a means of saving for every family's girl child. The SSY is valid for 21 years from the date of opening the account or until the girl reaches the age of marriage after reaching the age of 18.

National Strategy for Financial Inclusion

Apart from various schemes launched by the Government, the apex bank in India on its own has also devised the strategy for financial inclusion. The Reserve Bank of India (RBI) had devised a National Strategy for Financial Inclusion (NSFI) for the period 2019-2024. It is an ambitious strategy that aims to strengthen the ecosystem for various modes of digital financial services in all Tier II to Tier VI centres in order to build the infrastructure needed to transition to a cashless society. RBI identified six strategic objectives of a national strategy for financial inclusion:

- Universal access to financial services
- Providing basic bouquet of financial services
- Access to livelihood and skill development
- Financial literacy and education
- Customer protection and grievance redressal, and
- Effective coordination.

Microfinance Institutions

Microfinance institutions (MFIs) are financial companies that provide small loans to people who do not have any access to banking facilities. The definition of "small loans" varies between countries. In India, all loans that are below Rs.1 lakh can be considered as microloans. The different types of institutions that offer microfinance are:

- Credit unions
- Non-governmental organisations
- Commercial banks
- NBFCs
- Small Finance Banks
- Some government banks also offer microfinance to the eligible categories of borrowers.

Although most microfinance institutions target the eradication of poverty as their primary motive, some of the new entrants focussed on the sale of more products to consumers.

Goals of Microfinance Institutions

Microfinance institutions have been gaining popularity in the recent years and are now considered as effective tools for alleviating poverty. Most MFIs are well-run with great track records, while others are quite self-sufficient. The primary goals of microfinance institutions are the following:

- Transform into a financial institution that assists in the development of communities that are sustainable.
- Help in the provision of resources that offer support to the lower sections of the society. There is special focus on women in this regard, as they have emerged successful in setting up income generation enterprises.
- Evaluate the options available to help eradicate poverty at a faster rate.
- Mobilise self-employment opportunities for the underprivileged.
- Empowering rural people by training them in simple skills so that they are capable of setting up income generation businesses.

Key Benefits

The part that microfinance plays in economic development is noteworthy. Some of the key benefits of MFIs include the following:

- It enables people expand their present opportunities – The income accumulation of poor households has improved due to the presence of microfinance institutions that offer funds for their businesses.
- It provides easy access to credit – Microfinance opportunities provide people credit when it is needed the most. Banks do not usually offer small loans to customers; MFIs providing microloans bridge this gap.
- It makes future investments possible– Microfinance makes more money available to the poor sections of the economy. So, apart from financing the basic needs of these families, MFIs also provide them with credit for constructing

better houses, improving their healthcare facilities, and exploring better business opportunities.

- It serves the under-financed section of the society – Majority of the microfinance loans provided by MFIs are offered to women. Unemployed people and those with disabilities are also beneficiaries of microfinance. These financing options help people take control of their lives through the betterment of their living conditions.
- It helps in the generation of employment opportunities – Microfinance institutions help create jobs in the impoverished communities.
- It inculcates the discipline of saving – When the basic needs of people are met, they are more inclined to start saving for the future. It is good for people living in backward areas to inculcate the habit of saving.
- It brings about significant economic gains – When people participate in microfinance activities, they are more likely to receive better levels of consumption and improved nutrition. This eventually leads to the growth of the community in terms of economic value.
- It results in better credit management practices – Microloans are mostly taken by women borrowers. Statistics prove that female borrowers are less likely to default on loans. Apart from providing empowerment, microloans also have better repayment rates as women pose lesser risk to borrowers. This improves the credit management practices of the community.
- It results in better education – It has been noted that families benefiting from microloans are more likely to provide better and continued education for their children. Improvement in the family finances imply that children may not be pulled out of school for monetary reasons.

Leading Microfinance Companies in India

1. Equitas Small Finance

The lender offers small loans between Rs.2,000 and Rs.35,000 to the Economically Weaker Section (EWS) and Low Income Group categories in the country.

Loan Details:

Loan Amount	Interest Rate	Processing Fee
Up to Rs.25,000	24% p.a.	Nil
More than Rs.25,000	23% p.a.	1% + GST

2. ESAF Microfinance and Investments (P) Ltd.

ESAF Microfinance is a leading MFI in India that has empowered more than 4 lakh members through its 150 branches. It offers an extensive range of business development and financial services to the economically and socially challenged members of the society. The institution offers a bouquet of loan products to suit the varied needs of customers:

Loan Details:

Loan Amount	Rs.1,000 - Rs.1 lakh
Interest Rate	22% - 26% p.a. on diminishing basis
Processing Fee	1% - 2% of loan amount + GST
Loan Tenure	3 months – 60 months

3. Fusion Microfinance Pvt Ltd.

Fusion Microfinance is an RBI registered NBFC-MFI that works on a JLG lending model of Grameen. The institution offers loans to women in the rural and semi-urban regions. Apart from offering financial support and insurance protection, the company also imparts financial literacy to its customers.

Loan Details:

Loan Amount	Rs.3,000 – Rs.60,000
Loan Tenure	8 months – 2 years
Interest Rate	21% - 21.50% p.a. on reducing balance method
Processing Fee	0 – 1% of loan amount + GST

4. Annapurna Microfinance Pvt Ltd.

The purpose of Annapurna Microfinance is to provide loans to the financially underserved population. Technical and financial education is also imparted to beneficiaries to strengthen their entrepreneurial skills. It is one of the top ten NBFC-MFIs in India today.

Loan Details:

Loan Amount	Rs.1,500 – Rs.25 lakh
Loan Tenure	12 months – 240 months
Interest Rate	18% - 26% p.a. (reducing)
Processing Fee	1% - 2% + GST

5. Arohan Financial Services Limited

Eastern India's largest NBFC MFI, Arohan Financial Services Limited offers financial inclusion products to 1.9 million customers throughout India. The local partners of the company help in improving its reach to remote locations. Non-financial products are also offered by the company at affordable costs. Arohan also has an MSME lending business in its portfolio.

Loan Details:

Loan Amount	Rs.1,100 - Rs.50,000
Loan Tenure	3 months - 24 months
Interest Rate	20.70% - 21.25% p.a.

6. BSS Microfinance Limited

The company offers microloans to poor women so that they can be part of income generating activities that bring them out of poverty. The institution offers loans in the states of Maharashtra, Karnataka, Tamil Nadu, and Madhya Pradesh.

Loan Details:

Loan Amount	Rs.8,000 - Rs.60,000
Interest Rate	25% p.a.
Processing Fee	1% + GST (for loans above Rs.25,000)

7. Asirvad Microfinance Limited

This microfinance institution has an extensive network of branches throughout 22 states in India. It offers microloans to women entrepreneurs from low-income households for income generation activities. Currently, three types of loans are offered to borrowers, i.e., Product Loan, Income Generation Program (IGP) Loan, and Small and Medium Enterprise (SME) Loan.

Loan Details:

Loan Amount	Rs.2,498 - Rs.45,000
Loan Tenure	12 months - 24 months
Interest Rate	21.70% p.a.

8. Cashpor Micro Credit

Cashpor is a microfinance institution that works towards bringing the economically backward sections of the society out of poverty. The products offered by the company include credit facilities, savings services, insurance coverage, and pension services.

Loan Details:

Credit facilities offered by Cashpor is predominantly for undertaking income generation activities. Loans are also provided for non-income generation activities and acquisition of assets that improve the health and social status of the beneficiaries. For instance, loans for the construction of toilets, women empowerment, and the procurement of gas connections are commonly offered by the company.

9. Bandhan Financial Services Limited

The motive of the institution is to reduce socio-economic poverty by generating employment opportunities for low-income households. Cost-effective financial and non-financial products are provided in this regard.

10. Fincare Business Services Limited

The Fincare group consists of two NBFC-MFIs, i.e., Disha Microfin Ltd. (now referred to as Fincare Small Finance Bank) and Future Financial Services Pvt. Ltd. (FFSPL). The company caters to the semi-urban and rural households of the country, offering Microenterprise Loans (MEL) and loan against gold with quick disbursals.

2.2.4 Part D: Micro Finance: Concept, Characteristics, Need, Present Position in India

2.2.4.1 Introduction:

Microfinance is the provision of loans and other financial services to the poor. The microfinance has evolved due to the efforts of committed individuals and financial agencies to promote self-employment and contribute to poverty alleviation and provision of social security. India has been able to develop its own model of microfinance organizations in the form of savings and credit groups known as the Self Help Group (SHGs), which are bank-linked. These SHGs are mainly formed and managed by women and this has become an instrument, which has led to women's empowerment and social change. Most of the microfinance institutions in India attempt to go beyond savings and credit groups to provide microfinance services in the form of savings and insurance. Microfinance provides financial services to those whose income is small and unstable. These people are in need of credit facilities for several reasons (i) their needs are small and arise suddenly (2) the institutional providers of finance namely the banks demand collateral security which they cannot provide (3) most of the time, they are in needs of funds to meet their consumption demands, for example, to meet expenses related to education, illness, funerals, weddings for which it is difficult to obtain institution finance (4) for purpose of investment in income generating activities.

The Indian microfinance scene is dominated by SHGs and their linkage with Banks. Owing to the importance of microfinance and self help groups in the eradication of poverty and in the empowerment of women.

2.2.4.2 The Concept of Microfinance:

Microfinance is a concept that is helping the poor to avail of an create opportunities for economic growth. In India, microfinance has fulled the efforts of rural development, women empowerment and wealth generation by providing small scale savings, credit, insurance and other financial services to poor and low income households. Microfinance thus serves as a means to empower the poor and provides a valuable tool to help the economic development process. The concept of microfinancing and self-employment activities in rural areas has developed considerably over the last two decades. It is working neither on domain/charity nor on subsidy. It is basically rotational investment done to motivate the poor to empower themselves and practice the dictum 'Save for the future and use those resource during the time of need.' Theoretically, microfinance also known as microcredit or microlending means making provision for smaller working capital loans to the selfemployed or self-employment seeking poor. Microcredit has defined as the extension of small loans to be given in multiple doses based on the absorption capacity of the needy beneficiaries, who are too poor to qualify for formal bank loans, as they have no assets to offer as collateral security against loans. 'Microcredit' may be defined as the credit and repeated credit provided in small measures to suit the recipient's requirements, with a comfortable pace of repayment and at an appropriate rate of interest. Microcredit has been defined by the microcredit summit held in Washington D.C. in February 1997 as "programmes that provide credit for self employment, other financial and business services to very poor persons." Microfinance can be interpreted in a broader context both as microcredit and microsavings, even though microcredit and microfinance have come to used interchangeably. However, when the term 'microfinance' is used it implies some other services accompanying credit viz. facilities for saving and availability of services for insurance of the assets acquired with microcredit. Microfinance has come to be referred to as a small scale financial services and technical assistance provided to rural people who operate small or micro-enterprises, provide services, work for wages or commission and other individuals and group working at local levels. NABARD has defined microfinance as "provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semiurban and urban provided to customers to meet their financial needs; with only qualification that (1) transactions value is small and (2) customers are poor." In essence, therefore, microfinance could be referred to as an institutional mechanism of providing credit support in small amount and usually linked with small groups along with other complementary support such as training and other related services to the people with poor resources and skills for enabling them to take up economic activities. In the November 1995 Microcredit Summit, U.S. first lady Hillary Clinton wrote; "Microenterprise is the heart of development because microenterprise programmes work - they lift women and families out of poverty. It is called micro but its impact on people is macro, we have seen that it takes just a few dollars, often as little it takes as dollar 10, to help a woman gain self employment, lift her and her family out of poverty. It is not a hand out; it is a helping hand." Let us begin by understanding some of the distinct characteristics of microfinance. The term 'microfinance' is often confused with the related term 'microcredit', so much so, that the two are often treated as synonymous and used interchangeably. While there are certain similarities between the two terms, there are also certain differences, which require to be classified at the very start to avoid confusion of time. The term microcredit refers to a small size loan, to be repaid within a short period of time, used mostly low income households and micro entrepreneurs for the purpose of income generation and enterprise development. The mobilization of such credit is restricted to external sources such as banks and moneylenders. Microfinance on the hand, provides a greater menu of options whereby the small loan can be garnered not just from the external sources but also through selfmobilization, by way of saving and sale of assets. Also, in case of microcredit, due to the definite obligation to repay the loan, a physical collateral may sometimes be needed. However, the biggest flexibility in the case of microfinance is the lack of any physical collateral, even in case of loan from the bank. The options available with microfinance, therefore, are much broader and flexible than the ones available with microcredit

The Important Features of Microfinance

1. Microfinance is a tool for the empowerment of poor women;
2. Loans under microfinance programmes are very small;
3. Microfinance targets the poor rural and urban households;
4. Credit under microfinance follows thrift i.e. mobilize savings and lend the same;
5. Low transaction cost due to group lendings;
6. Transparencies in operation;
7. Short repayment period;
8. Simple procedure for reviewing, processing and approving loan applications and delivery credit;
9. Chances of misutilization are rare and there is assured repayment;
10. Peer pressure act as the collateral security required for loans;
11. Need based loan disbursement;
12. Prompt repayment; and
13. There is no ceiling from the RBI in respect of minimum and maximum amounts.

Microfinance is not a financing system but a tool for social change. It does not spring from market forces along - it is potentially welfare enchaining there is public interest in promoting the growth of microfinance - this is what makes it acceptable as valid goal for public policy.

2.2.4.3 Present Position of Microfinance in India :

The profile of microfinance in India at present can be traced out in terms of poverty. It is estimated that 350 million people live below poverty line. The following are some components of microfinance :-

(a) This translates to approximately 75 million households.

(b) Annual credit demand by the poor in the country is estimated to be about Rs. 60,000 crores. (c) A cumulative disbursement under microfinance programmes is only about Rs. 5000 crores. (d) Total outstanding of all microfinance initiative in India estimated to be Rs. 1600 crores.

(e) Only about 5% of rural poor have access to microfinance.

(f) Though a cumulative of about 20 million families have accepted accessed.

(g) While 10% lending to weaker sections is required for commercial banks; they neither have the network for lending and supervision on a larger scale or confidence to offer term loan to big microfinance institutions.

(h) The non poor comprise of 29% of the outreach.

2.2.4.4 Need for Microfinance:

Microfinance aims at assisting communities of the economically excluded to achieve greater levels of asset creation and income security at the household and community level. Access to financial services and the subsequent transfer of financial resources to poor women enable them to become economic agents of change. Women become economically self-reliant, contribute directly to the well being of their families, play a more active role in decision making and are able to confront systematic gender inequalities. Access to credit has been given considered a major poverty alleviation strategy in India. Micro-credit has given women in India an opportunity to become agents of change. Poor women, who are in the forefront micro-credit movement in the country use small loans to jump start a long chain of economic activity. Microfinance is accessing financial services in an informally formal route, in a flexible, responsive and sensitive manner which otherwise would not have been possible for the formal system for providing such services because of factors like high transaction cost emanating from the low scale of operation, high turnover of clients; frequency of transaction etc. Microfinance and self help group must be evolved to see that SHGs do not charge high rates of interest from their clients and improve access to those who cannot sign by their use through thumb impression. The current literature on microfinance is also dominated by the positive linkages between microfinance and achievement of millennium development goals (MDGs). Micro-credit Summit Campaign's 2005 report argues that the campaign offers much needed hope for achieving the millennium development goals especially relating to poverty reduction. IFAD along with food and agriculture organization

(FAO) and the world food programme (WFP) declared that it will be possible to achieve the eight MDGs by the establishing deadline of 2015 "if the developing and industrialized countries take action immediately by implementing plans and projects, in which micro-credit could play a major role."Credit is vital to the poor for overcoming the inevitable and common imbalance between income and expenditure. Credit is also crucial to the poor for income generating activities, like investing in their marginal farms or other small scale self-employment ventures. Their access to formal banking channels, however, is limited due to their low resource bases as well as due to the nature of formal credit institutions. The popularity of the microfinance, self help groups stems from widespread recognition that formal banking channels are largely ineffective in catering to the credit needs of the poor. Tiny savings and loans are generally an unattractive business proposition for formal banking institutions. In addition to disincentives faced by the banks, there are also problem faced by the poor in accessing loans from formal banking institutions. For example, to minimize risks, banks demand, collateral security that the average micro borrower does not possess. Banks also insist on complicated procedures that are too time consuming and often too complicated for the poor and illiterate. Even in the implementation of direct lending programmes formal institutions find it difficult to overcome the problem of targeting. The experience is that the rich and powerful typically manage to corner the scare loanable funds. Thus formal banking channels remain largely inaccessible to the poor in India. As a result, the poor continue to be dependent on informal sector lending, paying exorbitant rates or underselling the product and their labour power to the creditor. It was in response to these limitations in formal banking channels that micro credit mechanism were innovated. A quite from the former U.N. Secretary General Kofi Annan's video message on the launch of the international year of micro credit on 18th November 2004 also shows the significance of microfinance. "Microfinance has proved its value, in many countries, as a weapon against poverty and hunger. It really can change people's lives for the better - especially the lives of those who need it most. It is a way to extend the same rights and services to lowincome households that are available to everyone else. It is recognition that poor people are the solution, not the problem. It is a way to build on their energy and vision. It is a way to grow productive enterprise and so allow communities to prosper." In conclusion, it can be said that, it is a high time to focus on regulation for micro financing institutions in India.

2.3 Summary:

In the recent past, new weapons of investment have emerged in financial markets. Mutual fund is a collective investment vehicle which caters to the needs of small investors with lot of advantages. Similarly, investors with relatively higher funds need professional management of the fund and for that they are ready to bear the cost. For such investors, portfolio management services are provided.

On the other hand, some people even do not have access to formal banking services. They need these services at an affordable cost. Microfinance is an attempt in this direction. Still a lot needs to be done in this aspect. But with some coordinated efforts from banks, post offices and other intermediations, India can achieve the target of financial inclusion of all the people in rural and remote area.

2.4 Terms to Remember

- **Mutual Fund :** It is a financial intermediary that pools the savings of investors for collective investment.
- **Net Asset Value :** It is value of a fund reflect in the market minus liabilities on the day of valuation.
- **Portfolio Management :** Selection of securities and constant shifting of the portfolio in the light of varying circumstances.
- **Financial Inclusion :** Universal access to a wide range of financial services at a reasonable cost.

2.5 Check Your Progress

A) Fill in the blanks with appropriate alternative.

i) .... is known as a collective investment vehicle

a) Venture Capital b) Equity Share c) Mutual Fund d) Debenture

ii) Mutual funds have advantage of ....

a) Diversification b) Professional Management
c) Liquidity d) All of the above

iii) .... scheme of mutual fund has tax benefit.

a) Debt fund b) Balance fund c) Money market d) ELSS

iv) Combined holding of many kinds of financial securities i.e. shares, debentures, bonds etc. is known as ....

a) Microfinance b) Portfolio c) Venture capital d) Mutual fund

v) Only those who are registered with .... are eligible to operate as portfolio manager.

a) AMFI b) SEBI c) RBI d) All of the above

vi) RBI and Govt. of India have been making efforts to increase financial inclusion since ....

a) 1991 b) 2005 c) 2011 d) 2014

vii) Provision of loans and other financial services to the poor at affordable cost is known as ....

a) Financial inclusion b) Microfinance
c) Mutual fund d) Portfolio Management

viii) .... linkage programme resulted into women empowerment to some extent in rural area.

a) Aadhar b) SHG-Bank
c) Bank-Income Tax d) None of the above

B) Fill in the blanks

i) N.A.V. stands for ....

ii) .... schemes are open for investment during specific period only.

iii) In india, mutual fund industry started in the year ....

iv) Selection of securities and constant shifting of the portfolio in the light of changing circumstances is known as.................

v) ATM stands for ....

vi) Branch expansion, credit penetration and deposit penetration are dimensions of ....

vii) Credit for self employment, other financial and business services to poor people is ....

viii) SHG stands for ....

C) State whether the following statements are true or false.

i) Microfinance and microcredit are one and the same.

ii) UTI is considered as pioneer in Indian mutual fund industry.

iii) Balance fund has the features of both equity and debt fund.

iv) All mutual fund schemes have tax benefit.

v) Seeking high expected returns by avoiding risk in basis of portfolio management.

vi) Both merchant banks and investment banks provide fee based corporate advisory services.

vii) Providing credit at affordable cost is known as financial inclusion.

viii) Loans under microfinance are relatively low.

2.6 Answers to Check Your Progress

A) i) c ii) d iii) d iv) b v) b vi) b vii) b viii) b

B) i) Net Asset value ii) Close ended iii) 1964 iv) Portfolio management
v) Automated Teller Machine vi) Financial inclusion
vii) Micro Credit viii) Self Help Group

c) i) False ii) True iii) True iv) False v) True
vi) True vii) False viii) True

2.7 Exercise

A) Short Notes

i) Importance of Mutual Funds

ii) Objectives of portfolio management

iii) Need of financial inclusion

iv) Characteristics of microfinance

B) Answer in brief

i) Explain advantages of mutual funds

ii) Describe the concept of portfolio management

iii) Discuss the government policy towards financial inclusion

iv) Explain the need of microfinance in India

C) Broad Questions

i) What is mutual fund? Explain the present status of mutual funds in India.

ii) Explain the phasewise development of mutual fund industry in India.

iii) What do you mean by portfolio management? What are issues in construction of a portfolio.

iv) What are various types of portfolios?

v) Explain the progress of financial inclusion in India.

vi) What is micro finance? What is its present status in India?

2.8 Further Readings

i) Security Analysis and Portfolio Management - A. V. Avadluin

ii) Financial Institutions and Markets - B. L. Bhole

iii) Financial Management - I. M. Pundey

iv) RBI Report on Financial Indusion - RBI

v) Annual Reports - RBI

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Unit 3

Corporate Restructuring

Unit Structure

3.0 Objectives :

The study of this unit will enable students to

(i) Understand the concept of Corporate Failure

(ii) Know the Causes and Remedies of Corporate Failure

(iii) Understand the concept of Corporate Restructuring.

(iv) Know the Forms of Corporate Restructuring.

(v) Understand the financial restructuring and Strategic alliances.

(vi) Know the major corporate failure and Corporate Restructuring in India

3.1 Introduction:

Financial crisis is the main reason for restructuring the company. When any company suffers heavy losses consistently or having critical financial position may require restructure of its capital structure. If the company has potential to maximize profit in near future, then and then only the corporate restructuring is advisable.

Corporate failure means the inability of a corporate organization to fulfill its economic needs and attain its financial objectives as well as legal obligations. There are several factors which affected on corporate failure such as managerial inefficiency and ineffectiveness, economic instability, socio-cultural factors and public policies.

This topic emphasize the concept, causes and remedies of corporate failure as well as concept & forms of corporate restructuring, financial restructuring and strategic alliances.

3.2 Subject Matter:

3.2.1 Corporate Failure: Meaning

Corporate failure is very vital issue in view point of economist, bankers, creditors, share holders, marketing and management experts, financial and corporate managers etc. In simple words corporate failure means the inability of a corporate organization to fulfill its economic needs and attain its financial objectives as well as legal obligations. There are several factors which affected on corporate failure such as managerial inefficiency and ineffectiveness, economic instability, socio-cultural factors and public policies. The corporate failure may destabilize the economic system in various ways such as increasing unemployment and level of poverty, depriving people, increase in the rate of crime and tax earning may reduce. In accordance with these issues every corporate organization should continuously monitor their performance by establishing research and development department. In short Corporate failure means the inability to pay debts when they become due, the market value of assets of the firm is less than its total liabilities.

Corporate governance failure refers to situations where the management or the board of directors of a company fail to fulfill their legal and ethical responsibilities towards the company and its stakeholders, including shareholders, employees, customers, and the wider community.

Corporate governance can fail when the management or board of directors of a company do not adhere to ethical and legal standards, leading to poor decision-making and a lack of accountability.

Definition : "Corporate failure could be seen in terms of the inability of a corporate organization to confirm itself with its strategic path of growth and development to attain its economic and financial objectives as well as legal obligations." (David O. Mbat & Eyo I. Eyo, 2013)

From the above definition it is clear that corporate failure refers to companies operations following its inability to make profit or to earn revenue to meet out their routine expenses. There are three types of corporate failure such as.

1. A corporate body with low or negative return
2. A corporate body which is technically insolvent.
3. A corporate body which is bankrupt.

A body corporate which continuously earn very low profit or in loss is may fail because there is no opportunity for expansion in future. A corporate that is unable to meet its liabilities as and when due is technically insolvent. Where as a corporate who's total assets are less than total liabilities is bankrupt.

1. Causes of Corporate Failure

Generally any body corporate may fail because of hampered its ability to properly apply the financial resources which they have. Every corporate has a strategy to fulfill the demand of market and to generate maximum profit. However many organizations fail because of inappropriately formulated strategy or lack of it. There are several reasons / causes of corporate failure such as managerial inefficiency and ineffectiveness, socio cultural factors and economic instability which are discussed as follows.

A. **Managerial inefficiency and ineffectiveness:** It is the main cause of corporate failure. It consists of ineffective sales force, over expansion, high production cost inappropriate costing plan, low productivity, poor financial management, etc.

1. **Over expansion**: A corporate solvency is mainly depend upon the mobilization of short term funds. But the organizations which undertakes over expansion may not mobilize the short term funds properly and it is the cause of corporate failure. Hence corporate expansion should strictly follow the strategic plan.

2. **Ineffective sales force:** Profit may increase by way of increasing volume of sales. A stability of any organization is depends on cash flow which again depends on effective sale of production. If the sales force is not properly trained, it is difficult to sell its product effectively. This circumstances creates problem of cash flow and solvency problem.

3. **High Production Cost:** Now a day there is a cut throat competition in the market. To compete different product in the market it is necessary to control cost of production. But due to over employment, non-availability of proper material and technical inefficiency in the production process the cost of production may increase. It is the cause of corporate failure.

4. **Poor Financial Management:** The investment decision, financing and dividend policy decisions are mainly rely upon financial decisions. If financial manager is unable to take fast and effective financial management decisions is bound to experience acute liquidity problem.

5. **Lack of proper commercial policy :** The commercial policies affects the volume of sales which adversely affects the earning capacity of the organization. It creates the liquidity crises in organization.

6. **Risk Assessment Policy:** The investment in various sector particularly investment in assets constitute the most important source of corporate earnings. A corporate income would be hampered if risk assessment is not properly done.

7. **Lack of manpower training and development policy :**The achievement of corporate objectives are rely upon skilled and trained manpower. A corporate that does not have training and development policy cannot make the use of such well trained staff which create critical situation in the corporation.

B. Other Factors:

1. **Lack of Capital:** The undercapitalized body corporate is bound to fail sooner or latter. Due to lack of sufficient capital such companies faced problems regarding

buying the fixed assets, invest in proper income generating assets or enough working capital.

2. **Socio Cultural Factors:** The final aim of the organization is to sell the product which produced. If such product is not absorbed in immediate environment will have tough times selling its product. In such case organization look for another market which will lead to higher marketing costs and inability to sell its product.

3. **Public Policy:** It is most important external source of corporate failure. If government policies are against the interest of a corporate in a short term period, the corporate could go insolvent.

In addition to that following are the causes of corporate failure.

1. Failure to understand the market and customers.
2. Opening a business in an industry that is not profitable.
3. Failure to understand and communicate what the company is selling.
4. Inadequate financing
5. Reactive attitude
6. Overdependence on a single customer
7. Poor management
8. No customer strategy
9. No planning
10. Neglect of technology updating
11. Inertia to change

12. Neglect of research and innovation

13. Rely on few major customers,

14. Dishonest audit committees etc.

2. Remedies for Corporate Failure :

By considering all the above mentioned causes of corporate failure one can identify the cause and could be used to minimize its incidence. The institution of efficient and effective management is one of the most important measure to avoid corporate failure. Generally it includes the following factors.

1. **Managerial Training and development :** A performance and success of the corporate is depends upon the effective and efficient employees. Managerial Training and development policy make them improve on job performance.

2. **Improvement in productivity and business process reengineering:** Enhancement of productivity and business process reengineering consists of improvement in productivity, application of appropriate financial structure and increasing the level of competitive advantage in the market.

3. **Control the Various Variance :** Management should continuously monitor and control the various variance level such as a) Sales Price Variance, b) Sales Volume Variance, c) Sales Mix Variance, d) Sales Quantity Variance, e) Market Size Variance and f) Market Share Variance.

4. **Strategic Performance Measurement:** This is an accounting system used by top management to evaluate well known strategic business units.In addition to that

- Restructuring business activities
- Reducing debt burden
- Improving productivity, quality
- Strategic partnership
- Cost reduction and control
- Enhancing competitiveness
- Adapting to changing environment

- honest audit committee, and appointment of non executive directors are the some remedies for corporate failure.

For effectively carried out the various measures mentioned above to minimize corporate failure, a corporate body must have effective and functioning research and development department.

3. Major Corporate Failure in India

There have been several instances of corporate governance failure in India in recent years. Here are some of the top cases.

1. Kingfisher Airlines (KFA):

It is very difficult and challenging job to start an airline company, however, it is far more difficult to sustain it over time. Kingfisher was one of the biggest passenger airlines launched by flamboyant Vijay Mallya in 2003. It is also known as King of good times. They quickly rose to become the fifth-largest passenger airline in India, offering both domestic and international flights to passengers at flexible prices. Kingfisher also won the Skytrax award for being India's best airline in 2011.

Vijay Mallya, had extensive experience in the brewing industry. He has become known as a liquor baron. But, he lacked experience running businesses like airlines, despite his expertise in that field. As a result, he was unable to provide inspirational and effective leadership to the Kingfisher team which led to the failure of kingfisher airlines**.**

Currently Vijay Malia is in the UK and fighting battle in courts to stop his repatriation into India. Consortium of banks led by SBI has exposure of around Rs, 9000 crores to now a virtually bankrupt airline.

Because of failure of KFA most employees lost or quit jobs as salaries were nor paid for months together. The company went to the extent of defaulting in depositing statutory dues like PF, TDS deducted from salaries to government authorities.

Important reasons of Kingfisher Failure

- Acquisition of Air Deccan
- Expansion in The International Arena
- Lack Of Stability at The Apex Level of Management

- Switching from Premium Class Airline to the Low Budget Segment
- Increasing Cost of Fuel

In short, the team's inability to make good decisions has led to KFA's demise. The acquisition of Air Deccan, the service's rapid entry into the international arena, and its shift in segments, which prompted rivalry, were all important factors in its demise.

Vijay Mallay runs many businesses apart from breweries and KFA. The breweries were managed by experienced hands, so his liquor business flourished. However, due to his political and other business commitments he was not able to give proper attention on KFA.

2. The Punjab and Maharashtra Co-operative Bank (PMC Bank):

The Punjab and Maharashtra Co-operative Bank established in 1984. They received the designation of scheduled commercial bank in 2000. During the year 2018–19, its balance sheet is in excellent shape. RBI received a letter from a whistle blower informing the fraud. When RBI checks the accounts and the NPA data, the proportion of Gross NPA rose from 3.76% to 77%. The six senior bank employees are included in fraud and they prepare more than 20,000 fictitious accounts.

The bank was giving the business loans to 44 affiliated firms of HDIL. The bank continues to provide them money, even when they don’t pay back the loan. The entire amount borrowed, INR 6500 crores, was 4 times the regulatory maximum imposed on the bank and represented 73% of its assets.

During investigation, it was found that:

- As on 31st March, 2019 near about 70 % of its total loan book of Rs 8,383 crore, had been taken by real estate firm HDIL.
- The bank had been allegedly running fraudulent transactions for several years to facilitate lending to HDIL through fictitious accounts and violating single-party lending rules.

Effect on Economy and Society : PMC Bank failure was adversely affected on the Economy and Society. The reputation and credibility of cooperative banks were severely damaged due to PMC Bank failure. As a result, depositors may no longer have faith in and interest in the country’s banking system. Again it adversely affects the rate of capital formation and reduces the amount of money available for the country's economic growth.

Reasons of Failure: A conspiracy between politicians, property owners, and bankers paralysed the cooperative bank. Financial violations, breach of corporate ethics, violation of corporate governance (Waryam Singh served as a board member of HDIL while also holding the position of chairman of PMC Bank) , poor governance, Internal control and management system failure , Falsification of its financial statements *were* the main reasons of PMC Bank Failure

3. Failure of Infrastructure Leasing & Financial Services (IL&FS) :

Infrastructure Leasing & Financial Services (IL&FS) was a major infrastructure financing and development company in India. The company defaulted on its debt obligations, and it was later discovered that there were several irregularities and fraudulent activities within the company. The scandal led to a liquidity crisis in the Indian financial system.

Fraud occurred, in spite of marquee shareholders like LIC, SBI etc., being the largest shareholders, having representatives on board. ILFS had the largest debt exposure of around Rs. 91000 crores. It includes PF and pension funds.

Major reasons of failure:

- Diversion of borrowed funds to related entities of some of members of top management team
- Imprudent lending to parties who were not credit worth for ulterior motives
- Evergreening of loans by routing money from one group company to another through an unrelated party
- Over invoicing of project costs by vendors, accounting of fake expenses etc and difference being routed back to related entities of some of members of top management team
- Overstatement of profits by non- provisioning of loans, accounting of fake expense, inappropriate recognition of project revenue etc.
- The company had unprecedented number of subsidiaries and group companies, (346) which were used to route above transactions

- Non – disclosure of some of these companies as related parties
- Non-disclosure some of subsidiaries, associates, joint ventures

Due to the high credit rating of the company, most of the mutual funds, insurance companies and PF gratuity funds had invested large sums in its debt issuance. It was a case of negligence by reputed credit rating agencies that rating was not downgraded in spite of clear signs of financial stress in the company. Rating was downgraded abruptly to lowest level from the highest only after the company defaulted in its repayment obligations.

The government suspended the board and appointed eminent experts to the board chaired by reputed and seasoned banker, Uday Kotak. Currently the company is under resolution process and some of its infrastructure has been sold. However, progress has been slow. Hence, the extent and timing of recovery is uncertain.

4. Videocon Pvt. Ltd:

Videocon Industries was founded in 1979 by Venugopal Dhoot . Its headquarters in Mumbai. It initially started dealing in consumer electronics and home appliances such as mobile phones, colour TVs, air conditioners. After becoming a popular brand in these sectors, they became a conglomerate and diversified their business in Oil and Gas, Telecom, and DTH Services. The Videocon was the first company to launch colour TVs in India in 1982

The downfall of Videocon derives its traces from a time when there was an immense capital requirement in the television and allied sectors, but the returns were not adequate to control the debt. The company then tried to control their debts by divesting their business. They merged their DTH Services with Dish TV. They even sold their gas fields. Airtel acquired their telecom business. But, it was all too late to have any effect. Its downfall started with its decision to diversify its business into various sectors, by taking a lot of debt and not using leverage efficiently.

Main cause of Videocon failure

During 2012 there were too many irregularities in loans sanctioned by ICICI Bank. The authorities of the bank unofficially got a part of the loan from the promoter Venugopal Dhoot.

The CBI alleged irregularities in the acquisition of the 10% stake in the Golfinho-Atum oil and gas field by Videocon in 2008. The inquiry revealed that a consortium led by SBI sanctioned a loan of $2773.6 Million to Videocon for these bids. CBI alleged that the loan amount was siphoned to other accounts and businesses.

The company lost nearly Rs 21000 Crore in the 2G Spectrum Scam after its licences were revoked by Supreme Court in 2012. It made the telecom business unfeasible and forced it to sell the spectrum to Bharti Airtel, to recover damages to some extent.

Effect of Videocon failure

Shareholders of two listed companies of debt-ridden Videocon group will lose all money at the time of delisting as the liquidation values of the two firms are not even sufficient to cover outstanding debt.

Videocon was finally admitted to the NCLT for insolvency proceedings in 2018. The total claims among the different Videocon Group companies totalled a massive Rs 88000 Crore.

The Vedanta Group is taking over the insolvent Videocon Group. The Mumbai bench of the National Company Law Tribunal (NCLT) has approved Vedanta Group's Twin Star Technologies' resolution plan for beleaguered Videocon Industries Ltd. As per the resolution plan, Twin Star Technologies will pay Rs 2,962 crore against Videocon's total debt of Rs 31,000 crore.

Know Your Progress Part-I

A. Select the appropriate alternative

1. Corporate …………….. could be seen in terms of the inability of a corporate organization to confirm itself with its strategic path of growth and development to attain its economic and financial objectives as well as legal obligations.

   a) failure b) Restructuring c) Planning d) none of these

2. Corporate failure means the …………….to pay debts when they become due, the market value of assets of the firm is less than its total liabilities.

   a) ability b) inability c) recovery d) All of the above

3. Control the various …………level such as Sales Price Variance, Sales Volume Variance, Sales Mix Variance etc. is one of the remedial measures for corporate failure

   a) Variance b) Standard Deviation

   c) Mean d) Mode

4. Over .... is the cause of corporate failure.

   a) Time b) Confidence c) Expansion d) none of these

5. .... is most important external source of corporate failure.

   a) Private Policy b) Public Policy c) Life Policy d) All of the above

B. Write True or False

1. The corporate failure may destabilize the economic system in various ways such as increasing unemployment and level of poverty, depriving people, increase in the rate of crime and tax earning may reduce
2. Managerial inefficiency and ineffectiveness is the main cause of corporate failure.
3. Low Production Cost is also one of the cause of corporate failure
4. The fair capitalized body corporate is bound to fail sooner or latter.

C. Fill in the blanks

1. ……………….. refers to companies operations following its inability to make profit or to earn revenue to meet out their routine expenses.
2. Overdependence on a single ……………. is adversely affected on corporate.
3. Poor……………….. Management get corporate instability
4. Improvement in ……………….. and business process reengineering is essential to come out from corporate failure.

2. Corporate Restructuring : Meaning, Benefits

Financial crisis is the main reason for restructuring the company. When any company suffers heavy losses consistently or having critical financial position may require restructure of its capital structure. Many times the companies having bad financial position and suffering heavy losses may lead to dissolution or liquidation.

However corporate restructuring is the best alternative for liquidation as well as dissolution. It is mainly depending upon the assumption of that the company has the bright future and they can earn sufficient profit in near future. If the company has potential to maximize profit in near future, then and then only the corporate restructuring is advisable. If there is no hope for making sufficient profit in future, in such case the winding up of company is better than restructuring.

Restructuring means to rebuild or to reorganize. The term restructuring regarding companies refers to reorganizing the capital structure. The term corporate restructuring is defined as follows.

"Corporate Restructuring means reorganizing the capital structure of a company through reduction of claims of both the share holders and the creditors of a company or calling additional funds from share holders or creditors or both."

3.2.2.1 Forms of Corporate Restructuring:

Corporate Restructuring may be divided in to two types such as Internal Restructuring and External Restructuring. They are discussed as follows.

I) Internal Restructuring:

When capital structure of the company is reorganized by company internally it is called as internal reconstruction. It includes only reorganization of its own capital structure. The forms of internal restructuring are as follows.

1. **Alteration of Share Capital :** The right of alteration of share capital is provided by companies act 1956 to every company. Generally the share capital is altered by various ways such as i) Increase the share capital by issue of new shares ii) Cancellation of unissued shares iii) Conversion of fully paid shares into stocks iv) Consolidation of shares into larger denomination iv) Division of shares into smaller denomination. It is simple way of restructuring, hence it require ordinary resolution

2. **Reduction of share capital :** As stated above a company has right of alteration in share capital. According to companies act 1956, section 100 to 105 a company may reduce its share capital under corporate restructuring. Generally company may reduce share capital by i) The lost capital may written off; ii) Surplus share capital may refunded iii) The liability on uncalled share capital may reduced.

This type of reconstruction is generally requires special resolution of the general body and permission from the court. Before the reduction of share capital, company must be complete some legal formalities.

3. **Surrender of shares :** Under the scheme of corporate restructuring a company may surrender its shares. This type of reconstruction is also requires completion of necessary legal formalities. Under this system a part of share holdings is surrendered. Generally it includes i) For cancellation of shares some part of the share holdings are surrendered ii) Surrender of some of part of share holdings to some of the creditors.

4. **Divesture:** When any company sells its all the assets or sells its all business or branches to another company for cash is called as divestiture. Under divestiture all the assets i.e. fixed assets, current assets, raw material, work in progress, finished goods are sold to other company for consideration of cash as a lumpsum. Here, it is keep in mind that the purchase consideration may not be paid in other than cash such as shares, debentures or in any other form. To improve the goodwill in the stock market is one of the motives of the divestiture as well as to mobilize the resources for development of the organization.

5. **Buy-back of shares:** The main object of the buy-back of shares is to reduce excess capital of the company. It is one of the way of restructuring the existing organization. Under this system the company declares the scheme of buy back of its shares. The price for which the shares are to be taken back is determined by the company itself. The scheme of buy back is published in the regional as well as national newspapers. It includes price of the shares, opening and closing date of the buy back etc. Generally when excess capital found in company which remains idle, in such case company may return the cash i.e. capital to share holders by taking the shares back.

6. **Delisting of shares**: The SEBI regulates the stock market. It is beneficial to company to register or to enroll their shares in any stock exchange in India. It increases the reliance of investors. It helpful to attract the semi-conscious and small

investors. But in some cases a company may choose the way of delisting the shares for restructuring the capital structure of the organization. Generally it is not preferred by companies or very rarely adopted.

7. **Demergers:** It is the opposite term of merger. Demerger simply means splitting of the one company or business in to two or more companies. When any company sells or transfers its business or division of business to another one company or more than one company is called as demerger. Under this scheme the share holders of the existing company get the consideration of the demergers in the form of shares of the transferor company. For demerger the sanction of the existing share holders, as well as court and sanction of the SEBI is necessary.

II) External Reconstruction

When a company reorganized the capital structure with the help of external forms is called as external reconstruction. There are various forms of external reconstruction. They are as follows.

1. Mergers :

When two or more companies come together where one company survives and other company get merged into survived company. In this case one company may dissolved in another existing company and one company survives. All the assets and liabilities of one company are merged in to another existing company. Generally merger take place for the purpose of eliminating cut throat competition and to maximize profit earning capacity.

It may be of three types i.e. 1.Vertical 2. Horizontal 3.Conglomerate .

Vertical merger means combining two or more companies which are involved in related stages of production .e.g. weaving and spinning companies join together .

Horizontal merger means , two or more companies got merged in the same area of business . e.g. two T.V. companies join together.

When two firms engaged in unrelated lines of business merged , it is conglomerate merger .e.g. Chemical and fertilizer companies merge together .

Reasons for Merger :

Merger is form of external restructuring. Generally it is carried out for maximizing profits through eliminating competition among two similar types of companies.

1. **To Eliminate competition** : There is cut throat competition in the market. If it is avoided or eliminated the smooth progress of any business is possible. Generally the procedure of merger is take place for the purpose of elimination of this competition. It helps to reduce or eliminate this cut throat competition.

2. **To reduce cost** : Cost effectiveness is the *MANTRA* of the globalized era. Any organization must be careful about cost effectiveness. Cost of production and distribution cost is reduced to large extent with the help of merger. It is one of the important reason of merger to reduce cost and economy in the expenditure.

3. **To maximize profit** : It is one of the reason of merger. Mainly profit is depending upon cost effectiveness of product. If merger is take place the cost of production may reduce as well as competition is avoided which resulted in to maximization of profit.

4. **To survive in the market** : Due to cut throat competition in the market small and weak companies or organizations may collapsed and closed down. Therefore merger is the only way to survive in the highly competitive market .

5. **Economic stability**: The financial strength of one and single unit is less as compared to big unit. For increasing economic stability and financial soundness organizations may opt for merger. It helps to small organizations to expand their financial strength.

6. **Optimum utilization** : Optimum utilization of available resources is not possible to small and weak units. If such units merged into each other they can use these resources properly. Merger helps for maximum utilization of productivity and resources of the company .

7. **To increase competitive strength** : In the globalized era the competition is increased tremendously. To survive in the market it is necessary to increase the competitive strength of the organization. It is mainly possible with the help of merger. Merger leads to reduce the number of competitors.

8. **Expansion** : Merger is the way of expansion. For getting the benefit of large sale business merger helps to expand size of business.

Legal Procedure for Mergers

In merger two or more companies are willingly comes together. Generally merger takes place for elimination of competition and to maximize profit earning capacity of the organization. SEBI has controlled over these merger procedure. SEBI has laid down some guidelines and rules for mergers. However, the organization may completed some legal formalities regarding merger. It is as follows.

1. **Preparation of scheme of Merger** : First of all the top level management prepares the scheme of merger. It is the policy decision of the top level management. For this purpose they take the help of expert consultant. By considering Memorandum of Association of the company the team of expert prepares scheme of merger.

2. **Intimation to stock exchanges :** The stock exchanges where merging and merged companies are listed should be informed about the merger proposal. From time to time the copies of all notices, resolutions and orders should be mailed to the concerned stock exchanges. It is obligatory as per SEBI regulations.

3. **Approval of board of directors**: The formal approval of the BOD's of acquiring company is necessary. The draft merger proposal is submitted to the board of directors for its approval. It should be approved by the BOD's. They should pass resolution authorizing its directors and executives to pursue the matter further.

4. **Approval of Financial agencies :** The merging company should take the approval of the financial agencies i.e. bankers and lenders of the target company. For the approval of the merger the meeting of the financial agencies, banker, lenders and trustees of the debenture holders is arranged.

5. **Application to High Court :** Once the draft of the merger proposal is approved by the respective boards, merging and merged companies should apply to the high court of the state where its registered office is situated. High court approve the proposal and give direction to the acquirer company to call the meeting of the share holders of both the companies.

6. **Meeting of share holders** : The special general meeting of the share holders of both the companies are held to approve the scheme of merger. After approval of the

high court, the notice of the meeting should be dispatched to share holders and creditors of each company. The notice should be reached to them in such a manner that they should get 21 days advance intimation.

7. **Notice in newspaper** : The notice of the extra ordinary general meeting should be published in the leading newspapers. Such notice is also published before 21 days of the actual meeting.

8. **Holding of meeting :** A meeting of the share holders and creditors should be held by both the companies. The resolution of the scheme of merger is passed in this meeting at least by 75 % of share holders who votes either in person or by proxy. The same rule is applicable to creditors also.

9. **Petition to high court** : When the scheme of merger is passed in the extra ordinary general meeting of the share holders and creditors, both the companies should present a joint petition to high court for approval of the merger scheme.

10. **Filling the court order with the registrar** : The certified true copies of the high court order should be filed with the registrar of the companies. It must be filed with in the time limit specified by the court.

11. **Transfer of Assets and Liabilities** : After completion of all the formalities and final order –passed by both the courts , all the assets and liabilities of the target company are transferred to the acquirer company.

12. **Allotment of shares and Debentures;** After fulfillment of the provisions of the law the acquirer company should issues shares and debentures to the share holders of the target company. it means the share holders of the merged company become the share holders of the merging company.

13. **Application for Listing :** After issue of shares to merger company, the merging company submits the application for listing these shares in stock market. After completion of all the formalities the stock market listed the securities for trading purpose.

Examples of biggest merger :

i) Arcelor Mittal : In 2006, Mittal Steel announced its initial bid of $23 billion for Arcelor which was later increased to $38.3 billion. It is the biggest merger. This resulted in the new company Arcelor-Mittal controlling 10% of global steel production.

ii) Vodafone Idea Merger : Both the Vodafone and Idea companies struggled amidst the growing competition in the telecom industry. Particularly due to the entry of Reliance Jio and the price war that followed, these two companies decided to merge. The value of Vodafone Idea merger is $23 billion. The deal worked both for Idea and Vodafone as Vodaphone went on to hold a 45.1% stake in the combined entity with the Aditya Birla group holding a 26% stake and the remaining by Idea. The new identity of Vodafone Idea is marked as 'Vi'.

2. Amalgamation –

When two or more than two companies comes together and start a new company is called as amalgamation. It is combination of two or more companies and formation of new company. It means there are two or more liquidations and one formation. e.g. X Ltd and Y Ltd amalgamated and to form XY Ltd. In this case Vendor Company going into liquidation and new company is formed. Here XY Ltd to take over the business of X Ltd and Y Ltd. The business of vendor companies is taken over by new company on agreed terms and conditions.

3. Acquisitions –

When one company acquire or take over the business of another existing company is called as acquisition. Here a company which acquires the business of other company is knows as purchasing company or vendee company and other company is known as vendor company. It is also known as take over's. In this case acquiring company take overs the assets, net assets or stocks of another company. This company acquires control over another company directly by owing the assets or indirectly by obtained the control over management of that company.

Example of acquisition : Walmart Acquisition of Flipkart : Walmarts acquisition of Flipkart marked its entry into the Indian Markets. Walmart won the bidding war against Amazon and went onto acquire a 77% stake in Flipkart for $16 billion. Following the deal, eBay and Softbank sold their stake in Flipkart. The deal resulted in the expansion of Flipkart's logistics and supply chain network. Flipkart itself had earlier acquired several companies in the eCommerce space like Myntra, Jabong, PhonePe, and eBay.

4. Take over :

Take over means to make control over others by forcefully. Here, when one company forcefully taking over or acquiring the business of other company is known as take over. It is the popular form of reconstruction. It is external form of reconstruction. Takeover is the backdoor tool for control over the management and ownership. But as per SEBI's rules and regulations the backdoor takeover is illegal and it is treated as crime. Now it is compulsory to make PAN and Demat Account for purchasing the shares. Today takeover shall be only through front door. The SEBI prescribed legal procedure for take over. In India takeover can be only friendly and not hostile.

The take over come in to existence by following ways.

i. One existing company purchase the majority shares of another existing company from market.

ii. The creditors of the company may pressurize the existing company for take over.

It is also known as back door acquisition. However, SEBI has right to control over such practices.

Definition: "When one company takeover another company through acquiring control over the ownership and management of the another company by mutual agreement between both the companies."

Generally the takeover exists for eliminating the cut throat competition and to improve the leadership position in the market. The company which takeovers the other is known as acquirer company and other company is known as target company.

Benefits of Takeover :

1. Takeover means taking over the total business of the target company. It reduces the cut throat competition between target company and acquiring company.
2. It also strengthen the competiveness of the acquiring company.
3. Takeover helps t reduce cost of production.
4. It also helps to reduce cost of distribution and marketing.

5. The distribution channel of the targeted company is captured by acquiring company. It gives additional access to new distribution channel.
6. It gives boost to economy for their growth.
7. It helps to increase and expand the market and to attract the new customers.
8. It helps to optimum utilization of available natural as well as other valuable resources.
9. It helps to maximize the profit earning capacity of the acquiring company.
10. It is also beneficial to society and customers at large due to cost effectiveness of the company. They get product in time and at fair prices.
11. Takeoves makes financial position the acquiring company more sound.
12. It helps to overall development of the organization.

Example of takeover : Tata and Corus Steel : Tata's takeover of Corus Steel in 2006 was valued at over $10 billion. The initial offers from Tata were at £4.55 per share but following a bidding war with CSN, Tata raised its bid to £6.08 per share. Following the Corus Steel had its name changed to Corus Steel and the combination resulted in the fifth-largest steel making company.

Legal procedure for Takeover :

Today takeover shall be only through front door, back door takeover is treated as crime and heavy punishment is prescribed for it. Though the takeover is unwilling combination of two companies the SEBI prescribed legal procedure for it which is as follows.

1. **Appointment of Merchant Banker** : The top management takes the decision of takeover of the target company. After taking the decision of takeover the acquiring company may take the expert advice of the merchant banker. The SEBI classifieds the merchant bankers and as per SEBI's guidelines acquiring company may appoint the merchant banker from category-I.

2. **Collecting information** : After appointing the merchant banker, they collect the relevant and necessary information of the target company. Generally it includes information regarding production, market, distribution channels, share holders profile, debtors and creditors information etc.

3. **Submission of expert report :**The merchant banker prepares the expert advice report by considering all the important information as well as examining the memorandum and articles of association. It is submitted to top management of the acquiring company. The final decision of takeover is rely upon this report.

4. **Approval of the BOD :** The advice report submitted by merchant banker is first of all studied by top management and later on It is put before the Board of Directors of the acquiring company. The BOD approves the report and appoints a team of expert for formal negotiations with Target Company.

5. **Making negotiations:** The expert team makes formal and informal negotiation with Target Company. The details of the final negotiation are put on the paper. These final papers are signed by both the parties i.e. acquiring and target company.

6. **Make public announcement :** After the finalization of the negotiation of the takeover the acquiring company shall make public announcement within four days. It should be published in one National English or Hindi newspaper and one regional newspaper. This public announcement includes all the details regarding takeover.

7. **Preparation of Letter of Offer :** The acquiring company prepares the draft of the letter of offer. It contain offer price , mode of payment, date of payment, opening date of offer and closing date of offer etc. It is necessary to take approval of SEBI before sending this letter of offer to share holders of the target company.

8. **Approval of SEBI :**It is necessary to take approval of SEBI for takeover. For this purpose the acquiring company may submit letter of offer, MOU, documents of negotiations and other necessary papers to SEBI office with necessary fees.

9. **Letter of Offer to Target Company :** The final draft of the letter of offer is sent to target company for its consideration. It may be corrected with the consent of both the parties.

10. **Letter of Offer to Stock Exchange:** The approved and final draft of the letter of offer is then submitted to stock exchange where the shares of both the companies are listed. The submission of letter of offer to stock exchange is obligatory on the acquiring company.

11. **Letter of Offer to Share Holders :** The letter of offer approved by SEBI is then sent to share holders of the target company. This offer is optional and share holders of the target company may or may not be accept such offer. The offer remains open

for 30 days. The share holders who accept the offer should fill up the acceptance form and sent to merchant banker.

12. **Opening Account** : After sanction of the letter of the offer by share holders of the target company the offer price is paid to them. For the payment of offer price in the bank. the acquiring company opens the escrow account. The amount of offer price is deposited in to that account.

13. **Making payment and completion of takeover** : The acquiring company paid the offer price to the share holders of the target company through escrow account. Such payment must be paid within 30 days from the date of closure of offer and all the formalities of the takeover may complete within that period.

5. Joint Venture:

When two or more than two companies sharing the equity capital and advanced technology for carrying the business is called as joint venture. It is a partnership with other company in the form of equity capital and modern technology. Generally this partnership is made with foreign company. However under this reconstruction scheme the terms and conditions of joint venture may follow. In the era of globalization such type of reconstruction is popularized.

Examples of Joint Venture: I) The 2008 Joint venture of NBC Universal Television Group (Comcast) and Disney ABC Television Group (The Walt Disney Company). The objective of the joint venture was to create a video streaming application or a website named “HULU”. This product provides streaming quality content which is on computers, laptops or mobile phones. The product became a huge success with the offering lining upto $1 billion.

II) Another example of a joint venture is the joint venture between the taxi giant UBER and the heavy vehicle manufacturer Volvo. The joint venture goal was to produce driverless cars The ratio of the ownership is 50%-50%. The business worth was $350 million as per the agreement in the joint venture.

III) Vistra the joint venture between the Tata Son’s Group and Singapore Airlines where in this JV the majority of sake held by Tata Son’s with 51% and the rest 49% is under Singapore Airlines.

6. Demergers

Meaning :

It is the opposite term of merger. Demerger simply means splitting of the one company or business in to two or more companies. When any company sells or transfers its business or division of business to another one company or more than one company is called as demerger. The opposite of a merger, a demerger usually happens for the purpose of selling or liquidating a business unit, or empowering it to operate on its own as a separate legal entity. Under this scheme the share holders of the existing company get the consideration of the demergers in the form of shares of the transferor company. For demerger the sanction of the existing share holders, as well as court and sanction of the SEBI is necessary. Small businesses generally operate simply and thus are not in need of a demerger. However, when companies grow, their business structures become more complicated, consisting of multiple segments and business lines. This is when a demerger can be helpful.

A demerger can take place through a spin-off by distributed or transferring the shares in a subsidiary holding the business to company shareholders. The demerger can also occur by transferring the relevant business to a new company or business to which then that company's shareholders are issued shares of.

Definition :

According to Section 232 of Chapter XV of the Companies Act 2013, De-merger means split or division of a business or any undertaking of a company, making them separate units or undertakings. In short, de-merger means separation of a large company into one or more small companies.

A demerger is a form of corporate restructuring in which the entity's business operations are segregated into one or more components. It is the converse of a merger or acquisition. These units either operate on their own or are sold or liquidated as a divestiture.

A demerger allows a large company to split off its various brands or business units to invite or prevent an acquisition, raise capital by selling off components that are no longer part of the business' core product line, or create separate legal entities to handle different operations.

Types of Demergers

While there are a number of types of demergers, the following are the most common types of demergers.

1) Spin-Off

When a parent company receives an equity stake in a new company equal to its loss of equity in the original company, a spin-off demerger occurs. Latte on shares are bought and sold independently, and investors have the option of buying the most profitable shares. When the parent company retains a less-than-total stake in a demerged company, it is called as a partial demerger.

2) Split-Off

A split-off is a spin-off with more components. A split-off occurs when multiple businesses are split from the parent company into different entities. If the parent company is public, shareholders are given the option of trading in their shares for those of the newly created entities.

3) Liquidation Demerger

Liquidation demerger involves liquidating the business unit in question. Assets are divided among the new companies. Generally it happens when there are conflicts among management, board members, and shareholders about the direction of the business. It allows new companies to be created so that their visions can be met.

Reasons for demerging:

A demerger can help improve the financial performance of both the parent company and the newly created entities. By shedding underperforming or non-core assets, the parent company can improve its financial ratios and profitability. Following are the important reasons for demerging

1) Focus on core area

To make successful in the market, it is essential to focus on core competencies instead of various business streamline. A company may decide to demerge in order to focus on its core competencies and streamline its operations. A company may avoid the intension from non-core businesses or divisions. They can allocate more resources and attention to its primary and core areas of expertise.

2) Increase in financial performance

A demerger can help improve the financial performance of both the parent company and the newly created entities. By shedding underperforming or non-core assets, the parent company can improve its financial ratios and profitability.

3) Growth in strategic flexibility

Demergers can provide greater strategic flexibility. Each separate entity can pursue its own unique strategic goals, target markets, and growth opportunities. The broader organization's strategic direction can not disturb strategic flexibility.

4) Unlock shareholder value

By creating separate entities more attractive plans provided to share holders. It is possible through demergers. This can result in higher stock prices for the newly created entities, leading to increased shareholder value. That means demergers can often unlock shareholder value.

5) Compliance of regulations and law

Compliance of regulations and law is one of the important reasons of demerger of entity. In order to comply with competition laws or regulations that prohibits excessive market concentration. Changes in regulatory requirements or antitrust concerns may force a company to demerge.

6) Underperforming business units

Underperforming business units creates a drag on overall financial performance. They can be spun off, sold, or liquidated. Large entities, such as conglomerates, may be in need of streamlining, especially if they have made acquisitions. This may change or dilute their overall purpose and business plans.

7) Benefit of Strategic alliances

A company may pursue a demerger to facilitate strategic alliances or partnerships with other companies. Separate entities can enter into partnerships, joint ventures, or collaborations that are better aligned with their respective businesses

8) Tax efficiency

Demergers can sometimes be structured to achieve tax efficiencies. The separation of entities may lead to tax benefits that can enhance overall financial performance.

8) Investor demand

Many times investors make a demand to division of a company or express a preference for a particular business unit. In such case a demerger is helpful to meet investors demand. This allows investors to have a more direct and focused investment in the businesses they are interested in.

9) Reduce risk and complexity

In some cases, a company may demerge to reduce its exposure to risks associated with certain business units. To minimize risk and reduce complexity in the large conglomerates business units demerger is profitable. Separating risky or volatile assets from the core business can help protect the overall financial health of the company. Demerge simplify their corporate structure. This can lead to more efficient management and decision-making processes.

EXAMPLES OF DEMERGER

1. Tata Motors

Tata Motors Limited (TML) has approved the demerger into two listed entities – one for Commercial Vehicles (CV) and related investments, and the other for Passenger Vehicles (PV), Electric Vehicles (EV), and Jaguar Land Rover (JLR) businesses. This move follows the successful independent operation of these units under their respective CEOs since 2021. The demerger aims to enhance focus, agility, and accountability, capitalizing on distinct growth strategies. Limited synergies exist between CV and PV, but significant opportunities exist across PV, EV, and JLR, especially in EVs, autonomous vehicles, and vehicle software. Chairman N Chandrasekaran emphasizes the demerger's role in better capitalizing on market opportunities, improving customer experience, and driving shareholder value.

2. Reliance-Jio Financial

Reliance announced the demerger and subsequent listing of its financial services arm, Reliance Strategic Investments, as Jio Financial Services (JFS). Shareholders received one share of JFS for each share of Reliance held. The appointment of KV Kamath as non-executive chairman and Hitesh Sethia as CEO reflected the company's commitment to JFS's success. Analysts anticipated that JFS leveraging extensive data resources and a non-bank finance company license to venture into lending activities. This strategic move aligned with Reliance's goal of optimizing its structure to maximize shareholder value, focusing on the digital fintech sector's growth opportunities, and the value unlocking is in turn reflected in the increased share price of the company.

7. Divestiture

Meaning:

The term **'divestment' refers to** the **process of selling off a business or an asset class** that is **consistently failing** to meet the expectations of investors and other stakeholders. It is also known as divestiture. When any company sells it's all the assets or sells its all business or branches to another company for cash is called as divestiture. That means under divestiture all the assets i.e. fixed assets (it may be tangible or intangible) and current assets, raw material, work in progress, finished goods are sold to other company for consideration of cash as a lump-sum. However, the most important concept in divestiture is that, the purchase consideration may not be paid in other than cash such as shares, debentures or in any other form. One of the motives of the divestiture is to improve the goodwill in the stock market as well as to mobilize the resources for development of the organization.

Definition:

A divestiture i.e. divestment is the disposal of company's assets or a business unit through a sale, exchange, closure, or bankruptcy. Such disposal can happen partial or full. It is mainly depending on the reason why management opted to sell or liquidate its business' resources.

Divestment is the process of selling subsidiary assets, investments, or divisions of a company in order to maximize the value of the parent company. Also known as divestiture, divestment is effectively the opposite of an investment and is usually done when that subsidiary asset or division is not performing up to expectations.

Divestiture is the process of selling or disposing of a company's assets or business unit. It can be a partial or full disposal, depending on the reason for selling or liquidating the business' resources.

Selling intellectual property rights, corporate acquisitions and mergers, and court-ordered divestments are some of the examples of divestitures

A divestiture may occur if a business organization is deemed to be redundant after a merger or acquisition. It also occur when the disposal of a unit increases the sale value of the firm, or if a court requires the sale of a business unit to improve market competition.

Understanding Divestitures

To understand divestitures better, it is essential first to know the different types.

Carve-out

When a parent company sells one of its business units to another company is termed as a carve-out. The business unit can be sold fully or partly coming under carve-out.

Spin-off

When a company separates a business unit and forms a newly independent company from it is called as spin-off. When the company expects the newly independent entity to be worth more separately, in such case spin-off divestitures used. The spin-offs do not generate cash. However, to increase in shareholder value most of the companies adopted this type of divestitures as part of a strategy.

Split-off

This type is very similar to a spin-off. However, only difference is that the existing shareholders of the parent company have to choose between the two separate entities.

Reasons for **Divestitures**

Generally large public companies have more than one business unit under their organization. Hence in such companies divestitures are very common. Following are some of the most common reasons of divestitures,

1) Bankruptcy

Divestiture is one of the primary strategies to fight against bankruptcy. When a company is financially disturbed, in such case companies often sell unwanted or non-core assets. It helps to reduce costs and improving cash flow.

2) Raise Funds:

Every company wants to generate funds for a many reasons. It includes fund for investment and expansion or to pay off a big debt or heavy fine. Companies don't prefer to invest in subsidiaries or non-performing units during financially distressful times. In such case it is better to sell off the assets and save money to prevent insolvency. Divestitures are a great way to achieve liquidity.

3) Change in Strategy / Non-Core Assets

Generally every company has a 5-year business plan which lays out its road to success. When corporate strategies change, assets can sometimes become irrelevant or less important. In such case, companies can divest these non-core assets to reduce costs and distractions within the organization.

4) Underperforming Assets

There is a concept in Merger & Acquisition regarding the best owners of a business. Sometimes, a company needs to maximize the potential of a particular business and be deemed underperforming. There are potentially better owners of that business willing to pay more than what it's worth for the parent company.

5) Unlock Value

Companies also spin off business units because they can be more valuable as a standalone asset. Also, different parts of a company have different market values. As a result, investors might be willing to pay more for certain assets rather than the entire company.

6) Better Opportunities

An effective company always looks for good investment opportunities to create long-term value. There are instances when better opportunities arise and the companies need more cash to invest. Consider divesting a well-performing asset if it could generate more value for the company.

7) Stability in Stock Value

The share price is reflects the corporation's overall financial health. Hence, share price is most important to public companies. If an organization is involved in many industries through various business units, there could be instability due to market volatility. The company can choose to divest the asset involved in the volatile market to stabilize its stock price.

8) Political and social reason:

Companies may divest from certain assets due to political or ethical liabilities. e.g. the movement to divest from fossil fuels, or the movements to divest from geographies that are politically controversial, like Israel or Russia.

9) **Preventing Monopoly :**

For providing consumers options and control over prices , governments generally encourage competition in the markets. There have been instances when governments have made divestment mandatory for maintaining fair trade practices and avoiding a monopoly. If a company gets huge power and market share, regulators may force it to divest assets to restore balance.

Examples of Divestiture

Meta-Giphy Sale

In 2023, Meta (formerly Facebook) sold the animation database Giphy to Shutterstock for $53 million, which represented an 83% loss on what it paid for Giphy just three years earlier. The sale was forced by U.K. regulators, who believed that Facebook's acquisition of the gif-animation platform represented a violation of the country's antitrust laws.

Tata Power

A few years back, in 2018, to be precise, Tata Power divested a few of its non-core assets and came up with a plan for the growth and expansion of the next 10 years. The company planned to lay more emphasis on renewable power and services businesses. The officials of Tata Power stated that the growth and expansion of the business would take place in conventional power generation.

8. **Buyout:**

Generally Buyouts occur when purchaser believes a company's assets are undervalued and can be resold for a profit. In addition to that when purchaser believe that they will get financial and strategic benefits with the help of buyout , such as higher revenues, easier entry into new markets, less competition or improved operational efficiency, buyout come into existence. In finance, a buyout refers to the purchase of a company's voting stock in which the acquiring party gains control of the target company. A buyout can be funded with a combination of cash or debt.

When any purchaser purchase at least 51% of a company it is called as Buyout . Under a buyout, the previous ownership loses control over the company in exchange for compensation. In brief, a buyout is the purchase of a company's shares in which the acquiring party gains controlling interest of the targeted firm.

The company performing the leveraged buyout (LBO) may provide a small amount of the financing, typically 10%, and finance the rest through debt. The return generated on the acquisition is expected to be more than the interest paid on the debt. Therefore, high returns may be realized while risking a small amount of capital.

Examples of Buyout:

I. Hilton Hotels: In 2007, Blackstone Group bought Hilton Hotels for $26 billion through an LBO. Blackstone put up $5.5 billion in cash and financed $20.5 billion in debt. Before the financial crisis of 2009, Hilton had issues with declining cash flows and revenues. Hilton later refinanced at lower interest rates and improved operations. Blackstone sold Hilton for a profit of almost $10 billion.

II. Gibson Greeting Cards :In 1982, Wesray Capital acquired Gibson Greeting Cards for a purchase price of $80 million. The deal was financed with $1 million in cash, while the rest was borrowed by issuing junk bonds. After some time interval, Wesray sold Gibson Greeting Cards for $220 million, with investors earning about 200 times their initial equity invested.

Process of Buyout:

It may takes three to six months' time to complete a buyout procedure.

Generally buyout process is as follows.

1. Examination of Financial Documents : The purchaser examines the target company's balance sheet, income statement and statement of cash flows, and conducts a financial analysis on any subsidiaries or divisions seen as valuable.
2. Discussion with purchaser and target Company: After careful examination of Financial Documents , the purchaser and target begin discussing a buyout.
3. Offer of Buyout from Purchaser: The purchaser then makes an offer of cash and debt to the board of directors (BOD) of the target company.
4. Decision of Buyout: The decision of buyout i.e. whether to sell the business is decided by shareholders. The board either recommends the shareholders sell the buyer their shares or discourages the shareholders from doing so. They do not always welcome buyout offers. Therefore, buyouts may be friendly or hostile.

After completing the buyout process, the purchaser implements its strategy for restructuring and improving the company. The purchaser may sell divisions of the business, merge the business with another company for increased profitability, or improve operations and take the business public or private.

8. Strategic Alliance Meaning:

A strategic alliance is a relationship between two or more entities that agree to share resources to achieve a mutually beneficial objective. For example, a company manufactures and distributes a product in India and desires to sell it in other countries. Another company wants to expand its product line with the type of product the first company creates, and has a worldwide distribution channel. The two companies establish an alliance to expand the distribution of the first company's product.

That means, the two companies form a strategic alliance to pursue mutual benefits. Strategic alliances can develop in outsourcing relationships where the parties desire to achieve long-term win-win benefits and innovation based on mutually desired outcomes.

Definitions:

A strategic alliance is an agreement between two or more parties to pursue a set of agreed upon objectives needed while remaining independent organizations.

A legal agreement between two distinct organizations that provides for sharing resources collaboratively in pursuit of a mutually beneficial goal.

Example: The strategic alliance agreement between Monsanto and Grass Roots Biotechnology is a recent example of an alliance between a large company and small research-focused organization. Monsanto is a globally recognized agriculture company. Grass Roots Biotechnology is a small, research-oriented agricultural biotechnology company. The Monsanto/ Grassroots strategic alliance agreement called for Grass Roots to conduct research on Monsanto's behalf.

The strategic alliance between the Dutch airline KLM and the American carrier Northwest Airlines is a famous example of a strategic alliance that allowed two companies to share their routing networks but still remain distinct companies.

Benefits of Strategic Alliance

- Access to new technology and intellectual property rights,
- Diversification,

- To take Opportunities for growth
- Access to new market, new customers, to talent
- Improve agility, R&D, material flow, speed to market,
- Reduce administrative costs, R&D costs,
- To take competitive advantage of each partner.
- Reduce political risk while entering into a new market
- Access to new industries and reduce unhealthy competition
- To spur investments in innovation for Strengthening it.
- Partners in a Strategic Alliance can help each other by giving access to resources, (personnel, finances, technology)

Buy-Back of Shares

Buy-Back is a corporate action in which a company buys backs its shares from the existing shareholders. Generally company buys back its shares at a price higher than market price. It is also known as a share repurchase. Share or stock buyback is the practice where companies decide to purchase their own share from their existing shareholders.

It means a company buys its own outstanding shares from open market. Buyback of shares is carried out mainly either through a tender offer or through an open market. To reduce the number of shares available in the market and to increase the value of remaining shares available by reducing the supply is main objective of the Buy-Back of Shares. When number of shareholders reduces, it automatically reduces the controlling stake and increases the proportion of shares owned by investors. It is a system which allows companies to invest in them.

Buyback Process

Buybacks are carried out in two ways:

1. Open market : Companies buy back shares on the open market over an extended period of time. When companies decide to opt for the open market mechanism to repurchase shares, they can do so through the secondary market. They may prepare a programme of share repurchase through which shares are repurchases at certain times or at regular intervals.

2. Tender offer : Shareholders might be presented with a tender offer. Those who choose the tender offer can avail the same by submitting or tendering a portion of their shares within a given period at a higher price than current market price. This premium compensates investors for tendering their shares rather than holding onto them.

Reasons for buy-back:

Buy back of shares is an alternative mode of reduction in capital without requiring approval of the Court. When there is excess cash with company but there are not enough projects to invest in to them, in such case company decided to repurchase its own shares from open market. A company may feel its shares are undervalued and do a buyback to provide investors with a return is also one of the main reasons for buy-back. In addition to that there are some other important reasons why company buys back shares are summarized as follows;

- To improve earnings per share;
- To improve return on capital, return on net worth and to enhance the long-term shareholder value;
- To provide an additional exit route to shareholders when shares are under valued or are thinly traded;
- To enhance consolidation of stake in the company;
- To achieve a tax effective rewarding option
- To prevent unwelcome takeover bids;
- To return surplus cash to shareholders;
- To achieve optimum capital structure;
- To support share price during periods of sluggish market conditions;
- To service the equity more efficiently.
- To signal that the stock is undervalued
- A share repurchase demonstrates to investors that the business has sufficient cash set aside for emergencies and a low probability of economic troubles.

- To offer rewards and options, companies buy back shares and issue them to employees and management. This helps avoid the dilution of existing shareholders.

Impact of Share Buyback:

The shares buyback may affect different financial aspects of a company. They are highlights as follows;

1. **Effect on Earnings Per Share (EPS)**

When a company repurchases its own shares from open market, it reduces the total number of outstanding shares. However, the net income of the company remains the same as it is before the repurchasing of the shares. It lays a direct impact on its Earnings Per Share (EPS) by increasing the ratio significantly.

2. **Effect on Financial Statement**

The expenses incurred on repurchase of shares would be recorded in the business's earnings report. It is also recorded in the statement of cash flow as well as the statement of retained earnings.

Besides influencing the income statement of a company, the impact of share buybacks can be noticed in other financial statements as well.

Further, in the Balance Sheet, the total assets may reduce with equivalence of cash used for repurchase of sharers. Simultaneously, the amount of share capital would also undergo a reduction. This situation of reduction would help improve performance metrics like Return on Equity (ROE) and Return on Asset (ROA).

3. Effect on Increasing Shareholder Value

The companies who opt for buyback of shares are more likely to increase their earning per share (EPS) significantly. Besides, EPS enhance too much faster than operational improvements. It improves return on capital; return on net worth and in turn to enhance the long-term shareholder value. The practice of share repurchase helps to project a positive image of the company in the market, because it is believed that companies who are capable enough to repurchase their shares from shareholders have a grand market presence and robust pricing power.

4. Effect on the Company's Portfolio

Usually, companies who have faith in their prospects indulge in the practice of repurchasing their company shares. Such a display of confidence is received positively by potential investors and existing shareholders and helps earn their trust significantly. In turn, it helps the company to enhance its market reputation and facilitates an increase in its share value naturally. All of this directly helps improve the venture's portfolio significantly.

Example of a Buyback

For instance, share (stock) price of a company has underperformed its competitor's stock even though it has had a solid year financially. In such case, to reward investors and provide a return to them, such company announces a share buyback program to repurchase some amount of its outstanding shares at the current market price.

The company had Rs. 1 crore in earnings and 10 lakh outstanding shares before the buyback, equating to earnings per share (EPS) of Rs.10. Trading at a Rs.200 per share stock price, its P/E ratio is 20. With all else being equal, 100,000 shares would be repurchased and the new EPS would be Rs.11.11, or Rs.1 Crore in earnings spread out over 9,00,000 shares. To keep the same P/E ratio of 20, shares would need to trade up 11% to Rs. 22.22.

Know Your Progress Part II

A. Select the appropriate alternative

1. Under divestiture form, the consideration is to be paid in ……………… Only.

   a) shares   b) debentures   c) cash   d) bonds

2. Buy back of shares is a   form of restructuring.

   a) Internal   b) External   c) middle   d) None of the above

3. Under demergers form, the consideration is to be paid in the form of …………Only.

   a) Equity shares   b) debentures   c) cash   d) bonds

4. Merger is the form of   reconstruction.

a) Internal b) external c) middle d) none

5. Alteration of share capital require resolution

   a) Ordinary b) extra ordinary c) both d) none

6. Generally ……………. occur when purchaser believes a company's assets are undervalued and can be resold for a profit.

   a) Amalgamation b) Absorption

   c) Buyouts d) None of these

7. ………………is the process of reshuffling or reorganizing the financial structure of a company.

   a) Financial restructuring b) Financial Failure

   c) Alteration of share capital d) None of these

8. Buy back of shares lays a direct impact on its Earnings Per Share (EPS) by …………..the ratio significantly.

   a) Increasing b) Decreasing

   c) Both a and b above d) None of these

9. Buy back of shares is an alternative mode of reduction in capital without requiring approval of the ……………

   a) Shareholders b) Court

   c) Debtors d) Creditors

10. Buybacks are carried out in two ways i.e. ………and Tender offer

    a) Open market b) Close market

    c) Indian market d) Foreign market

B. Write True or False

1. Financial crisis is the main reason for restructuring the company.
2. Demerger is External form of restructuring.
3. In India, Takeover is hostile form of reconstruction.
4. SEBI has controlled over merger procedure.

5. Restructuring means to rebuild or to reorganize

6. Buyout is the purchase of a company's shares in which the acquiring party gains controlling interest of the targeted firm.

C. Fill in the blanks

1 .... is the best alternative for liquidation as well as dissolution.

2. When capital structure of the company is reorganized by company internally it is called as……………….

3 .... means to make control over others by forcefully.

4. When any company sells its all the assets or sells its all business or branches to another company for .... is called as divestiture.

5 .... simply means splitting of the one company or business in to two or more companies.

6. When any purchaser purchaseat least 51% of a company it is called as ………….

7. Debt restructuring is the process of reorganizing the whole .... capital of the company.

Practical:

Prepare and presentation of latest cases of corporate restructuring

Case No. 1: Three-way amalgamation of Vijaya Bank, Dena Bank and Bank of Baroda

On 1st April, 2019, Bank of Baroda, Vijaya Bank and Dena Bank were merged in a three-way amalgamation. In this amalgamation, 2,135 branches of Vijaya Bank and 1,777 branches of Dena Bank were merged with that of Bank of Baroda. The government of India announced the merger on 17thSeptember, 2018.In September 2018, the 'Alternative Mechanism' (AM) headed by Finance Minister Arun Jaitley had decided to merge Dena Bank and Vijaya Bank with Bank of Baroda. The basic aim of merging is to create a stronger and sustainable global-sized lender.

Type of Reconstruction :Three-way amalgamation

Name of the Companies :Vijaya Bank, Dena Bank and Bank of Baroda,

Who merged: Vijaya Bank and Dena Bank merged with Bank of Baroda

When : The government of India announced the merger of Bank of Baroda, Vijaya Bank and Dena Bank on September 17, 2018 and actual implementation is take place on 1st April, 2019,

Why : The decision of merging is taken to create the country's third largest ,a stronger and sustainable global-sized lender.

Effects of Reconstruction :

What happens to Vijaya Bank and Dena Bank shares after merger?

According to the Scheme of Amalgamation, shareholders of Vijaya Bank will get 402 equity shares of BoB for every 1,000 shares held.

In the case of Dena Bank, its shareholders will get 110 shares of BoB for every 1,000 shares held.

Conclusion:

On 25th May 2020, Bank of Baroda completed IT integration of 132 branches of the former Vijaya bank. On 1st April, 2019, Bank of Baroda, Vijaya Bank and Dena Bank were merged in a three-way amalgamation. In this amalgamation, 2,135 branches of Vijaya Bank and 1,777 branches of Dena Bank were merged with that of Bank of Baroda.

The migration process started after the payment channels of both the Vijaya bank and Dena Bank were merged with Bank of Baroda. After integrating ATMs, NEFT, RTGS, IMPS and UPI with BoB, merging of the branches of Vijaya Bank marked the start of the merging process.

While the IT integration of Vijaya Bank’s 152 branches is completed with 20 branches that had been migrated earlier, bringing it to the same IT platform, Finacle 10, as that of Bank of Baroda, the IT integration of Dena Bank is expected to be completed by end of this year or January 2021.

Case No. 2 : Merger (horizontal merger) of Allahabad Bank (Kolkata-headquartered) and Indian Bank (Chennai headquartered).

Both lenders had a rich legacy that went back to the pre–independence era. Indian bank with 113 years and Allahabad Bank with 155 years will create an institution with sound financial strength and nationwide connectivity consisting of 6,000-plus branches, 4,800-plus ATMs, 43,000-plus employees serving 120 million-plus customers and business mix of over Rs 8 trillion. Allahabad Bank had a total business of Rs.3.77-lakh crore as on March 31, 2019. Deposits were at Rs. 2.14-lakh crore, while advances were close to Rs.1.63-lakh crore. Indian Bank's total business stood at Rs.4.29-lakh crore with deposits of around Rs.2.42-lakh crore and advances of Rs.1.87-lakh crore.

All branches of Allahabad Bank will function as branches of Indian Bank following the amalgamation of the two lenders as per Reserve Bank of India (RBI)'s notification dated March 28, 2020. Effective April 1, Allahabad Bank will cease to exist in its present form and will be officially merged with Indian Bank.

Type of Reconstruction : Merger (horizontal merger)

Name of the Companies: Allahabad Bank Kolkata-headquartered and Indian Bank Chennai headquartered

Who merged : Allahabad Bank merged into Indian Bank, Indian Bank will retain its name after its merger with Allahabad Bank

When : April 1, 2020

Why : As on March 2019, Indian Bank and Allahabad Bank's combined business is estimated to be close to Rs. 8-lakh crore. Their branch network put together is close to 6,104. They have a plan to expand the total branches of the merged entity to 10,000 and register Rs.10-lakh crore business in another two to three years. Bank will make the new entity the seventh-largest bank in India. The increased lending capacity shall be utilised to serve Corporate and MSME clientele

CEO /Chairman :Managing Director and CEO of Indian Bank : Padmaja Chunduru, Managing Director and CEO of Allahabad Bank : S.S. Mallikarjun Rao

Effects of Reconstruction: Allahabad Bank will cease to exist in its present form and will be officially merged with Indian Bank. The bank would continue to deliver top-grade products and services to all its old customers. None of the branch is going to be closed. Only those branches that are just adjacent to each other will be combined. Both banks have a common core banking platform, BaNCS, developed by TCS.

A fair equity share exchange ratio of 115 equities of Rs. 10 each for every 1000 shares of Rs.10 of Allahabad Bank as a part of the amalgamation.

Conclusion : The merger of Kolkata-headquartered Allahabad Bank and Chennai-based Indian Bank will make the new entity the seventh-largest bank in India. Indian Bank is the anchor bank in this merger process. At the end of the third quarter this fiscal, the combined business of the two banks stood at Rs 8.44 lakh crore with a total of 6,104 branches. Indian Bank's business stood at Rs 4.29 lakh crore with 2,887 branches as on December 31, 2019, while Allahabad Bank's total business as on December 31 last year stood at Rs 3.77 lakh crore with 3,175 branches. Bank will make the new entity the seventh-largest bank in India.

Case No. 3 : Joint Venture of Tata Steel and ThyssenKrupp

Tata Steel and Thyssenkrupp (TK), a German multinational conglomerate, have signed a deal to merge their European steel operations. As per the final terms of the deal, each company shall hold a 50% stake in the new venture, known as Thyssenkrupp Tata Steel B.V. This merger is set to become the second-largest steel company in Europe, only behind Arcelor Mittal. The company is expected to have a labour force of around 48,000 workers.

Type of Reconstruction : Joint Venture

Name of the Companies: Indian steel major Tata Steel and German giant ThyssenKrupp

When : September 2017

Why : According to investment bankers, both Tata Steel and Thyssenkrupp are facing a tough financial situation and will take steps to sell some assets so that they can meet Europe's anti-competition norms. Since June 2017, steel prices have crashed and the financial metrics of both companies have deteriorated.

In the past few years, Tata Steel Europe has not performed very well due to high competition in Europe, weak global conditions and cheap Chinese imports in the market. All of these factors resulted in a negative Profit after Tax (PAT) of Rs 304 crore for Tata Steel in 2017. The merger with TK and Tata Steel Europe's restructuring activities in the past year could help improve operational performance.

CEO /Chairman : ThyssenKrupp CEO Heinrich Hiesinger, Tata Steel chairman Natarajan Chandrasekaran

Capital ratio : 50: 50

Effects of Reconstruction

- What this means for Tata Steel

The joint venture (JV) could help Tata Steel to reduce leverage and focus on creating a strong Indian platform in the European market. This deal would reduce Tata Steel Europe's debt by Rs 20,000 crore or €2.5 billion.

- What this means for Thyssenkrupp

The performance of Thyssenkrupp was better than Tata Steel after the MOU was signed in September 2017. The joint venture between Tata Steel and Thyssenkrupp could result in sales equal to Rs 13 lakh crore ($ 19.9 billion). In addition, the joint synergies of both the companies could help them to realise additional significant value of around Rs 40,000 crore (€5 billion) for each company.

Conclusion :

The merger between Tata Steel and TK is expected to have a positive impact on Tata Steel's shareholders. The merger could contribute around Rs 57,000 crore to Tata Steel's consolidated financials. The merger with TK and Tata Steel Europe's restructuring activities in the past year could help improve operational performance. This could benefit shareholders' prospects. After murger, Tata Steel's stock price increased by around 10% in view of the merger. According to CEO of TK the joint synergies of both the companies could help them to realize additional significant value of around Rs 40,000 crore (€5 billion) for each company

Case No. 4 : Merger of Idea Cellular and Vodafone India(merger of two equals)

It was announced in March 2017 that Idea Cellular and Vodafone India would merge. The merger got approval from Department Of Telecommunications in July 2018. On 30 August 2018, National Company Law Tribunal gave the final nod to the Vodafone-Idea merger. The merger was completed on 31 August 2018, and the newly merged entity was named Vodafone Idea Limited. The merger created the largest telecom company in India by subscribers and by revenue. Under the terms of the deal, the Vodafone Group holds a 45.2% stake in the combined entity, the Aditya Birla Group holds 26% and the remaining shares will be held by the public. Vodafone Idea lost a significant number of gross and active subscribers in the month of August 2020 after the merger. The nature of both the companies are as, Vodafone

– a postpaid & Prepaid GSM service and Idea – a prepaid GSM service, similar to Vodafone Prepaid.

Type of Reconstruction: Merger

Name of the Companies: Vodafone India Limited and Idea Cellular

Name after Reconstruction: Vodafone Idea Limited ('VI')

When: The merger was completed on 31 August 2018

Why: The two companies decided to merge their business after the sector witnessed a huge tariff war and reduction in margins with entry of new telecom operator Reliance Jio and to create the country's largest telecom company with 408 million active subscribers and a revenue market share of 32.2%., the merged entity could be the biggest telecom company in India. It would have nearly 40 crore customers, 35% customer market share and 41% revenue market share. Months ago, the entry of Reliance Jio in the market disrupted the operations of other service providers. This merger is a strategic response to Jio's significant move.

Capital Ratio : Equal (1:1)

Effects of Reconstruction: **Effect on Shareholder**

The two companies agreed to merge their operations with a swap ratio of 1:1. This means every Idea share you hold will be exchanged with a new share in the merged company. This suggests that operationally, it is a merger of two equals.

However, an independent valuation of the two businesses suggests Vodafone's business is worth more. The assessment suggests Vodafone India's business is worth Rs 82,800 crore, while Idea's business is valued at Rs 72,200 crore. However, Idea's shares fell 14% after the announcement of the deal. This is because investors were not clear about the deal despite a detailed announcement. The price of ABN shares fell as much as 25% post the announcement.

To maintain an equal partnership, Vodafone will have 45.1% stake in the combined company. This is after transferring a 4.9% stake at Rs 110 per share to Aditya Birla Group for Rs 3,900 crore in cash. Aditya Birla Group will then own 26% of the combined company. The remaining 28.9% will be owned by Idea shareholders. The Birla Group will have the right to buy additional 9.5% stake from

Vodafone over the next 4 years. This is to ensure that both the companies have an equal stake in the new company.

Conclusion :

The two companies agreed to merge their operations with a swap ratio of 1:1. It is a merger of two equals. The merger is very fruitful and profitable to both the companies, but shareholders did not take the merger announcement well. Therefore, Idea's shares fell 14% after the announcement of the deal. This is because investors were not clear about the deal despite a detailed announcement. The price of ABN shares fell as much as 25% post the announcement. Shares in Grasim did not fell as much. However, they corrected by 10% before the announcement when the merger rumors started. One reason for this could be that the numbers don't tally. The merger equals 10 shares of ABN with 3 shares of Grasim. However, 10 shares of ABN cost Rs 12,880, while 3 Grasim shares are worth Rs 13,602.

Case No. 5 :Acquisition of Sun Pharma and Ranbaxy Laboratories About Sun Pharma:

Sun Pharmais established by Dilip Shanghvi in 1983. Its headquarter is in Mumbai.It is an international, integrated, specialty pharmaceutical company. It manufactures and markets a large basket of pharmaceutical formulations as branded generics as well as generics in India, the US and several other markets across the world. In India, the company is a leader in niche therapy areas of psychiatry, neurology, cardiology, diabetology, gastroenterology, orthopedics and ophthalmology. The company has strong skills in product development, process chemistry, and manufacturing of complex dosage forms and APIs. Over 72% of Sun Pharma sales are from markets outside India, primarily in the US. Manufacturing is across 26 locations, including plants in the US, Canada, Brazil, Mexico, and Israel. Sun Pharma was listed on the stock exchange in 1994. Today Sun Pharma is the second largest and the most profitable pharmaceutical company in India, as well as the largest pharmaceutical company by market capitalization on the Indian exchanges.

Sun Pharma made 13 acquisitions between the 1997 and 2012, starting with the purchase in 1997 of Detroit-based Caraco Pharmaceutical Laboratories. That was the year in which it also bought stakes in two Indian pharma firms—Tamilnadu Dadha Pharmaceuticals Ltd and MJ Pharmaceuticals Ltd. In 2010, it acquired a majority stake in Israel-based Taro Pharmaceutical Industries, a move that more than doubled its revenue in the US to $1.1 billion from $484 million. Within two years, Sun Pharma bought two more drug makers in the US—Dusa Pharmaceuticals Inc. and the generic business of URL Pharma Inc.

About Ranbaxy Laboratories:

Ranbaxy is established in 1961 and headquartered in Gurgaon. It is an integrated, research based, international pharmaceutical company producing a wide range of quality, affordable generic medicines, trusted by healthcare professionals and patients across geographies. Ranbaxy's continued focus on R & D has resulted in several approvals in developed and emerging markets, many of which incorporate proprietary Novel Drug Delivery Systems and technologies developed at its own labs. The company has further strengthened its focus on generics research and is increasingly working on more complex and specialty areas. Ranbaxy serves its customers in over 150 countries and has an expanding international portfolio of affiliates, joint ventures, and alliances, ground operations in 43 countries and 21 manufacturing facilities spread across 8 countries. Ranbaxy is a member of the Daiichi Sankyo Group. Daiichi Sankyo is a leading global pharma innovator, headquartered in Tokyo, Japan. Daiichi Sankyo Co Ltd, Japan holds approximately 63.4% stake in the company. Ranbaxy went public in February 1973. Daiichi Sankyo acquired controlling in Ranbaxy in 2008 from its earlier promoters Malvinder Mohan Singh and family. Singh resigned in 2009 after Ranbaxy posted losses and after

Daiichi Sankyo decided to get more actively involved in the newly acquired Indian unit.

Type of Reconstruction: Acquisition

Name of the Companies: Sun Pharma and Ranbaxy Laboratories

Who acquired : Sun Pharmaceutical acquired 100% of Ranbaxy Laboratories

When: In April 2014, Sun Pharmaceutical acquired 100% of Ranbaxy Laboratories for $4 billion and completed the acquisition process on 25th March 2015.

Why: To create world's fifth largest specialty generic pharma company is the main objective of this transaction. The Ranbaxy has been incurring a net loss and suffering a decline in net worth since 2011. These include the settlement amount of US$ 515 million paid to the US Department of Justice (DOJ) in May 2013 after civil and criminal charges were brought against it for misrepresentation of data and irregularities found in two of its facilities in India, diminution in the value of its investments and a loss on foreign currency option derivatives. Thus, the merger of the company with Sun Pharma comes at a crucial time when Ranbaxy is struggling to improve its financial position.

Conclusion

The combination of Sun Pharma and Ranbaxy will create fifth-largest specialty generic company in the world and the largest pharmaceutical company in India. A combined Sun Pharma and Ranbaxy will have a diverse, highly complementary portfolio of specialty and generic products targeting a spectrum of chronic and acute treatments.

Sun Pharma has followed a strategy of acquiring poorly performing companies and turning them around. The merger won't have too many cultural and integration issues since both companies are Indian. Besides, an all-stock deal, Sun Pharma has also been able to avoid any open offer possibility to the minority shareholders. Given the large diversified operations of Ranbaxy and potential synergy benefits, we find the transaction more value accretive for Sun Pharma shareholders. Ranbaxy shareholders will receive 0.8 of a share of Sun Pharma for each Ranbaxy share.

3.3 Summary:

Corporate failure means the inability of a corporate organization to fulfill its economic needs and attain its financial objectives as well as legal obligations. There are several factors which affected on corporate failure such as managerial inefficiency and ineffectiveness, economic instability, socio-cultural factors and public policies.

When any company suffers heavy losses consistently or having critical financial position may require restructure of its capital structure. Restructuring means to rebuild or to reorganize. The term restructuring regarding companies refers to reorganizing the capital structure. Corporate Restructuring may be divided in to two types such as Internal Restructuring and External Restructuring. Corporate restructuring includes Buyouts, Financial restructuring and Strategic Alliance also.

When any purchaser purchases at least 51% of a company it is called as Buyout. In brief, a buyout is the purchase of a company's shares in which the acquiring party gains controlling interest of the targeted firm. Financial restructuring is the process of reshuffling or reorganizing the financial structure, which primarily comprises of equity capital and debt capital. Financial restructuring is not only a tool used by companies that are in financial trouble. Healthy companies may also choose to restructure their debt if it will provide a benefit. If interest rates fall, a company may refinance its loans to take advantage of this drop. A strategic alliance is a relationship between two or more entities that agree to share resources to achieve a mutually beneficial objective. Access to new market, new customers, to talent, new industry, new technology and to reduce competition, cost of production and to enhance the business are the major reasons for strategic alliance.

Though, financial crisis is the main reason for restructuring the company, healthy companies may also choose to restructure their debt if it will provide a benefit.

3.4 Key words:

1. **Corporate Failure :** It refers to companies operations following its inability to make profit or to earn revenue to meet out their routine expenses.
2. **Strategic Performance Measurement :** This is an accounting system used by top management to evaluate well known strategic business units.
3. **Restructuring :** To rebuild or to reorganize
4. **Merger :** When two or more companies come together where one company survives and other company get merged into survived company
5. **Takeover :** when one company forcefully taking over or acquiring the business of other company is known as take over
6. **Divestiture** : When any company sells its all the assets or sells its all business or branches to another company for cash is called as divestiture.
7. **Demerger :** it means splitting of the one company or business in to two or more companies.
8. **A strategic alliance :** is a relationship between two or more entities that agree to share resources to achieve a mutually beneficial objective.
9. **Financial restructuring :** is the process of reshuffling or reorganizing the financial structure
10. **Buyout :** means when any purchaser purchase at least 51% of a company

3.5 Answers of Know Your Progress Part I

A) a) failure 2. b) inability 3. a) Variance 4. c) Expansion

5. b) Public Policy

B) 1. True 2. True 3.False 4. False

C) 1. corporate failure 2. customer 3. Financial 4.productivity

Answers of Know Your Progress Part II

A) 1. Cash 2. Internal 3. Equity shares 4. External

5. Ordinary 6. Buyouts 7. Financial restructuring

8. Increasing 9. Court 10. Open market

B) 1. True 2. False 3.False 4. True 5.True 6. True

C) 1. Corporate restructuring 2. internal reconstruction

3. Take over 4. cash 5. Demerger 6. Buyout 7. debt

3.5 Exercise:

A. Short Answer / Notes:

1. What is corporate failure?
2. Explain the internal forms of corporate restructuring.
3. Explain the external forms of corporate restructuring.
4. State the benefits of Takeovers
5. What do you mean by strategic alliance?
6. Explain the term financial restructuring.

B. Short Notes:

1. Benefits of Takeovers
2. Internal forms of corporate restructuring
3. External forms of corporate restructuring
4. Merger
5. Takeover
6. Strategic alliance
7. Financial restructuring

C. Long answer type questions:

1. Explain the forms of corporate restructuring.
2. What is merger ? State the legal procedure for mergers.
3. Explain the legal procedure of takeover.
4. What is takeover? Explain the benefits of takeover.
5. Explain the term Strategic Alliance and state its advantages.
6. Explain the concept financial restructuring.

D. Prepare and presentation on latest five cases of corporate restructuring

3.6 Books for Additional Reading

1. Corporate mergers, amalgamation and Takeover – Varma J.C.
2. Corporate Finance - S.C.Kuchal
3. Essentials of Business Finance –Dr.R.M.Shrivastav
4. Business Finance – Chaudhari, Mankar, Shinde5. Corporate Restructuring and Indian Perspective – Matoo P.K.
6. Financial restructuring, Naveenkumar and TarunVenai
7. Corporate Financial Restructuring, Prof. Ian H. Giddy, New York University
8. Avika Mukherjee, Buy Back of Shares, Article on Web Site

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Unit 4

Recent Trends in Business Finance

Unit Structure

4.0 Objectives:

After studying this Unit the student will be able to

1. Aware about recent trends in business finance scenario.
2. Understand the concept and application of Startup Funding, Angel Financing and FinTech services.
3. Enhance the professional knowledge and skill related to recent trend in finance.

4.1 Introduction:

Government of India launched Startup India Scheme on 16th of January, 2016 with a slogan ‘Start-up India Stand-up India’. This scheme aims to foster startup culture and create innovative and entrepreneurial ecosystem in order to transform India into a job creator country. Now India has become one of the largest startup ecosystems in the world. Simple compliance regime, launching mobile applications and portals for compliance and exchange of information, legal support, fast tracking patent examination at reduced costs, faster exit opportunities, tax exemptions for three years and tax exemptions on capital gains, funding support and incentives are some of the features of Startup India.

4.2 Presentation of subject matter

4.2.1 Startups Funding

Startup India is a Government Scheme started to help entrepreneurs having innovative business ideas. Though entrepreneurs have innovative idea, many of them who want to start their own business lack the resources. At the early stage of growth of an enterprise every entrepreneur need enough capital.

Finance is life-blood of any organisation. Startups require funds for various purposes such as for purchase of inventory, office spaces, manufacturing a product, developing a product, expansion of business, sales and marketing activities etc. Startup funding is funding that startups get to establish or support or grow its business.

Startups are in need for sustained funding access throughout various stages. Newly started startups need money or funding for purchase of inventory, manufacturing a product, covering marketing activities, paying operating expenses etc. Sometimes, existing startups require funds for product development, expansion of business etc. There are various sources of funding for startups depending upon their need.

4.2.1.1 Fund raising norms for startups

To give boost for startups SEBI, the capital market regulator has introduced fund raising norms in 2015.

1. SEBI has relaxed the norms for startups for raising capital and opened the doors for raising the funds by Initial Public Offer.
2. According to new norms approved by SEBI's board, the stock exchanges should have a separate Institutional Trading Platform (ITP) for helping in capital raising by the startups.
3. According to SEBI norms Institutional Trading Platforms will be made accessible

a. To those companies which provide products, services or business platforms with substantial value addition.

b. These companies should have at least 25% of the pre-issue capital being held by Qualified Institutional Buyers(QIBs).

c. To those companies which make use of technology, information technology, intellectual property, analytics, biotechnology, nano-technology. The entire pre-issue capital shall be locked up for a period of 6 months from the date of allotment.

4. ITP platform is also available to those companies which are having at least 50 per cent of the pre-issue capital held by Qualified Institutional Buyers.

5. The person holding 25% or more than 25% of the post-issue share capital individually or collectively with persons acting in concert is disallowed by SEBI.

6. The entire pre-issue capital shall be locked up for a period of 6 months from the date of allotment.

7. The companies who want to list on the proposed ITP should have to file draft with documents with SEBI.

8. In some cases, the standard valuation parameters such as Private equity, Earning Per Share etc may not be relevant.

9. Institutional Investors (which comprises QIBs as per SEBI Regulations, 2009 along with family trusts, systematically important NBFCs registered with RBI and the intermediaries registered with SEBI all with net-worth of more than Rs. 500 crore) and Non Institutional Investors (NIIs) other than retail individual investors can access the proposed ITP.

10. Allocation between Institutional Investors and Non Institutional Investors shall be in the ratio of 75% and 25% respectively.

11. In the case of discretionary allotment to institutional investor, no institutional investor shall be allotted more than 10% of the total issue.

12. The minimum application size in case of such issues shall be Rs. 10 lakhs and minimum trading lot shall be of Rs. 10 lakhs.

13. In case of public offer the number of allottees shall be 200 or more.

4.2.1.2 Schemes available for new startups by Government in the form of Finances:

Government of India is providing various incentives for the growth of Startups. Startup India scheme aims at assisting financially the aspiring entrepreneurs. These entrepreneurs after getting approval from Department of Industrial Policy and Promotion powered by DPIIT the Startup India scheme offers them financial assistance in the form of loans and subsidies. The growth of Startups creates employment and helps in the development of National economy.

Following are the some important Government schemes available for New Startups –

1. Atal Innovation Mission (AIM)
2. Startup India Seed Fund Scheme
3. Startup India Initiative
4. MUDRA Yojana
5. SAMRIDH Scheme
6. The Venture Capital Assistance Scheme
7. Credit Guarantee Fund Trust for Micro and Small Enterprises
8. Raw Material Assistance Scheme
9. The Standup India Scheme
10. MSME Market Development Assistance (MDA)
11. Trade Related Entrepreneurship assistance and development (TREAD) Schemes for Women
12. Duty exemption and Remission Scheme
13. Sustainable Finance Scheme
14. 4E(End to End Energy Efficiency) Scheme
15. Dairy Processing and Infrastructure Development Fund

1. Atal Innovation Mission (AIM) –

The Atal Innovation Mission scheme was launched by NITI Ayog in 2016 to give exposure to young innovators and startups. AIM is initiative to generate a culture of innovation and entrepreneur, through this mission programmes and policies for innovation in various sectors of economy are developed. It has provided opportunities for collaboration and a stage for different stake holders. Through this mission a grant up to Rs. 50 Lakhs has been given to startups for developing a minimum usage prototype between nine months and one year.

2. Startup India Seed Fund Scheme –

The startup India Seed Fund Scheme was launched on 16 January 2021 for helping startups and supporting ideas from aspirant entrepreneurs. The idea behind this scheme is that, no startup in India will face shortage of capital. The objective of Startup India Seed Fund Scheme is to provide financial assistance for proof of concepts, proto type development, product trials, market entry and commercialization of products. This scheme helps Startup to get investments from Angel investors, Venture Capitalist or get loan from commercial banks or financial institutions. The eligible incubators distributes seed funds to eligible startups.

For validation of proof of concept or prototype development or product trials, the startups may get grants up to Rs. 20 Lakhs. For market entry, commercialization or scaling up through convertible debentures or Debt linked instruments the startups can get investment up to Rs. 50 Lakhs.

3. Start up India Initiative –

The Start up India Initiative is one of the important Government Scheme for startups in India. There is extensive collection of e books, courses and mentorship programmes to promote leadership and skills. Other benefits of the scheme include

- Tax exemption
- Access to Funds
- Cost Reduction
- Business windup option in Ninety days
- Fast track patient registration

- Fast track patient registration with eighty percent fee rebate

For getting funding for this scheme the startup should be registered as partnership firm, private limited company or Limited Liability Partnership.

4. MUDRA Yojana –

The Micro Unit Development Refinance Agency (MUDRA) loan for business startups is one of the important source of finance. To give financial assistance help Micro and small enterprises this scheme was launched. The person having the age between 18 to 65 years can get MUDRA loan. Traders, shopkeepers, vendors from rural as well as urban areas can can get this type of loan without any collateral or third party security. The small and medium businesses can get loan amount up to Rs. 10 Lakhs as per the MUDRA loan eligibility for startups. This loan is offered for startups through non-banking financial companies (NBFCs). There are three types of MUDRA loans, named as Shishu, Kishor and Tarun.

- **Shishu** – This type of loan is given for the startups in their initial stage, to get their business started. In this category the startups can get loan up to Rs. 50 Lakhs. The startups may use this amount for building infrastructure, purchase of asset or purchase of raw materials.
- **Kishor** – The startups who want to expand the business or grow further can get loans between Rs. 50,000/- to Rs. 5 Lakhs.
- **Tarun** – Under this loan scheme the startups can get loan amount between Rs. 5 Lakhs to Rs. 10 Lakhs. If the startup fulfills the required eligibility conditions, it can get the highest loan amount, which is Rs. 10 Lakhs.
- The interest rate changes as per RBI guidelines issued time to time.

5. SAMRIDH Scheme –

Startup Accelerator of MeitY for Product Innovation, Development and Growth (SAMRIDH) gives assistance to existing and upcoming accelerators to select and accelerate startup to scale. Through SAMRIDH scheme, funding up to Rs. 40 Lakhs is provided to the startups through the selected accelerators for extending their accelerator services.

6. The Venture Capital Assistance Scheme –

If there is shortage of capital for implementation of the project, then financial assistance is provided in the form of interest free loans to the eligible projects. The loans are provided by Small Farmers Agribusiness Consortium (SFAC).

7. Credit Guarantee Fund Trust for Micro and Small Enterprises –

Credit Guarantee scheme for startup provides credit guarantee up to particular limit to finance eligible startups against loan extended by MIs. This scheme provides collateral free debt funding to startups.

Under this scheme the eligible starup has to approach MI for credit assistance. The MI examines the project from different aspects and sanction need based assistance to the startup according to guidelines. Startups which are sanctioned by DPIIT under Gazette notification issued from time to time can get guarantee coverage up to Rs. 10 Corer per startup under the scheme.

8. Raw Material Assistance Scheme –

The Raw Material Assistance Scheme provides credit based financing to MSMEs to purchase Raw material (both indigenous and imported). This scheme helps MSMEs to focus on manufacturing of quality products. The benefit of this scheme is that it gives credit support for procurement of raw materials up to 180 days.

9. The Standup India Scheme –

The Standup India loan scheme provides bank loans to scheduled castes, scheduled tribes, and women entrepreneurs. All scheduled commercial banks and their branches will be covered under this scheme directly or through SIDBI standup India portal through the lead district manager. Under this scheme the banks will provide loans to eligible entrepreneurs from Rs. 10 lakh to Rs. 1 crore.

10. MSME Market Development Assistance (MDA) -

To increase the participation of MSMEs representatives in the international exhibitions or fairs this MSMEs Market Development Assistance scheme was introduced. It also provides financial assistance to use Global Standards (GS1) in barcoding.

4.2.1.3. SEBI Regulations on startup listing and fund raising

In December, 2108 BSE has launched the startup listing platform to allow deserving startups to raise capital from the market. The startup company intending to list on BSE Startup platform should be in the sector of Information technology, Biotechnology, 3D printing, Holographic, Information Technology Enabled Services, Space Technology, Hi-Tech Defense, Nano Technology, e Commerce, Artificial Intelligence, Drones, Virtual Reality, e Gaming, Genetic Engineering, Exoskeleton, Variable Computers Inside Body, Computer Technology and other High Technology based companies.

1. Track Record:

For listing on BSE the company or the proprietor or the partnership firm or the Limited Liability Partnership firm or the firm which have been converted in to the company should have a combined track record of minimum two years at the time of filing the prospectus with BSE.

2. Paid up Capital:

The company should be registered with Department for Promotion of Industry and Internal Trade as Startups. Those companies who are not registered with DPIIT as startup should require minimum paid up capital of Rs. 1 crore for listing with BSE.

A. Post issue paid up Capital

a) The post issue paid up capital of the company shall be less than Rs. 25 crore.

b) At the time of filing of draft prospectus with BSE, there should be preferably investment by qualified institutional buyers (QIBs)/angel investors/accredited investors for minimum period of 2 years.

B. Net Worth: The company should show positive net worth.

C. Other Requirements

a) The company must have website.

b) It is mandatory for the company to make arrangement of trading in Demat securities.

c) The company should enter into an agreement with National Securities Depositories Ltd.(NSDL) and Central Securities Depositories Ltd. (CDSL).

d) Prior to one year of filing of application for listing under startup segment on BSE, there should not be any change in the company's promoters.

D. Disclosures:

Promoting company should give certificate stating that

a. It has not been referred to National Company Law Tribunal (NCLT) under Insolvency and Bankruptcy Code , 2016.

b. No any director/promoter of the company has been debarred by any regulatory agency.

c. There should not be any petition against the company regarding winding up that has been accepted by the NCLT.

4.2.1.4 Venture Capital Vs Private Equity

1. Venture Capital

Venture Capital is a type of financing that is provided to startups and small companies having exceptional growth potential in long term. Venture capital is in the form of private equity. It provides funding to new companies or ventures with limited operating history (under two years) which does not raise capital through stock markets and do not have sufficient cash flow to operate. Venture capitalists provide assistance to such companies in the form of capital financing and technical or managerial expertise.

Venture capital funds are handled by professional managers. In addition to their own fund, these managers invest other people's funds. In other words, this investment is professionally managed with an expectation of getting good return on their investment in long run.

2. Private Equity

Private equity is a method of financing in which investor buys a stake in a private company, with a expectation of increase in the value of their stake. Sometimes, the unlisted companies cannot raise funds through issue of equity or debt instruments. So, these companies go for private equity for fund raising. In other words, private equity refers to a capital investment that is not listed on a public stock exchange.

Private equity shares can be acquired directly from an issuing company. They have high risk and are not liquid. It facilitates companies to acquire direct investments from private equity for long term. These funds are received from wealthy investors, pension funds, labor unions etc, The ultimate goal of private equity is to sell the stake in the company at added value. Private equity funds involve General Partner, Limited partners and target companies.

3. Comparison between venture capital and private equity

1. Meaning

Venture capital is type of financing in which finance is provided for such startups companies or small businesses having high growth potential and having ability to earn above-average returns in long run. Private equity refers to capital investment that is raised from private sources in which the investor intends to increase the value of its stake.

2. Size of Investment

Investment in venture capital is smaller than private equity. Initially, between $ 1 million to $ 10 million. Investment in private equity is typically larger than venture capital. It may be from $ 5 million to billions of dollars depending upon target company.

3. Structure of Investment

Venture capital is in the form of equity. Private equity firms may raise funds through the combination of equity and debt.

4. Types of Companies

In venture capital the investment is in startups in technology, biotechnology, information technology having high growth of potential. In private equity the investment is in stable, established companies which are already performing well.

5. Stage of Investment

Venture capital investments are made at initial or early stage of company. Private equity investments are made at the late stage of company.

6. **Focus on**

In venture capital the major focus is on management capability, innovation, disruption and rapid growth. In private equity the major focus is on corporate governance, operational efficiency and profitability

7. **Risk Involved**

As venture capital investment is made at early stage of high technology companies it involves high risk. As private equity investment is made in stable and established companies it involves less risk compared to venture capital.

8. **Fund required for**

In the case of venture capital the funds are needed for scaling up business operations. In the case of private equity funds are needed for growth and expansion of business.

9. **Focus of Investment**

In the case of venture capital investors may distribute the risk by investment in many different businesses. In the case of private equity investors focus on fewer investments at one time.

10. **Return Profile**

In venture capital there are higher risk investments with broader set of outcomes from home runs to total loss of investment. In private equity the returns are more stable than venture capital.

11. **Scope**

Venture capital is a subset of private equity. Private equity comprises of leveraged buyouts, private placement along with venture capital.

12. **Exit Strategy**

Private equity exit strategies often include Initial public offers, mergers, acquisitions or secondary buyouts. Venture capital exit strategies often include initial public offers or acquisitions.

Check your progress -1

A) Select the appropriate alternative from among given below each statement

i) In the case of fund raising for startups, the minimum number of allottees for public offer shall be -----.

a) 200 b) 300 c) 150 d) 201

ii) SEBI has simplified the framework for capital raising by technological startups on ----- .

a) Investors Trading Platform b) Imaginary Trading Platform

c) Institutional Trading Platform d) Individual Trading Platform

iii) The Atal Innovation Mission Scheme was launched by ----- in 2016.

a) SEBI b) NITI Ayog

c) Planning Commission d) Finance Commisson

iv) The Startup India Scheme was launched on -----.

a) 16 January, 2016 b) 26, January, 2016

c) 15 August, 2015 d) 15 August, 2016

v) ------ scheme was launched to create innovative and entrepreneurial ecosystem in India.

a) Financial Inclusion b) Vishwakarma

c) Indira Awaas d) Startup India

B) State True or False.

i) Credit Guarantee Fund Trust for Micro and Small Enterprises requires collateral security for funding to startups. .

ii) In private equity the investment is in stable, established companies.

iii) Venture capital is subset of private equity.

iv) It is not necessary to have a website for the startup company intending to list on BSE Startup platform .

v) The maximum limit of loan amount under MUDRA yojana is Rs. 10 lakhs.

4.2.2 Angel Funding

Angel funding refers to an investment by angel investors for providing financial backing for small businesses. These are high-net-worth investment. Angel investment is a form of equity financing. Angel funds invest in the early stage of the business. These funds provide seed capital and intends to strengthen the startups.

Angel funding includes high risk so angel investors expects high returns for their investments. In India Angel funds are regulated by SEBI.

4.2.2.1 Origin of Angel Funding :

In old days for theatrical production, the required money was provided by the rich individuals. The money provided by the wealthy persons were returned back with interest after starting of productions generating revenue or in the form of equity. The term 'Angel' used to individual money providers in connection with Brodway theater.

The term 'Angel' was used in 1978 by William Wetzel who was professor at the University of New Hampshire and founder of the Center for Venture Research. He used the word 'Angel investor', when he completed his study on entrepreneurs, who raised capital for business. He used the term in connection with the investors who supported Startup businesses with seed capital.

At the initial phase these type of funding was generally done by executives or retired entrepreneurs who may be interested to invest in another generation of entrepreneurs. The money provider is an Angel, who provides funds in the early stage of business. Angel investors, generally use their own net worth. Their aim is to finance startup business in exchange for equity. Small business entrepreneurs or startups prefer Angel investors, because they are least obtrusive. Based on the companies size, an angel investor invests suitable amount which is helpful to the startup entrepreneur. Generally angel investor invests 5-10 percent of total fund available, in one company. In India, angel investors try to acquire an accredited investment status but this is not a prerequisite, it is a formal designation. The other names used for angel investors are angel funders, informal investors, private investors, business angels and seed investors.

4.2.2.2 SEBI Regulations on Angel funding :

These regulations are called the Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012.

These regulations came into force on the date of their notification in the Official Gazette 21 May 2012.

Definition:

Angel Fund - a sub category of Venture Capital Fund under Category I-Alternative Investment Fund that raises funds from angel investors and invests in accordance with the provisions of SEBI regulations.---SEBI Regulatins, 2012. Angel Investor is a person who intends to invest in an angel fund should satisfy following conditions, which are

a) An Individual investor having assets excluding value of his principal residence, of at least Rs. 2 crore, who has previous investment experience or serial entrepreneur or a person having minimum 10 years of professional experience in management.

b) A body corporate who has a net worth of minimum Rs. 10 crore.

c) An AIF a venture capital fund registered under SEBI (VCF) Regulations, 1996 or AIF registered under these regulations.

4.2.2.3 Registration of Angel Funds

As an angel fund it is necessary to apply for registration accordance with the provisions of SEBI Regulations.

Already registered AIF may apply for conversion to convert its category as an angel fund.

4.2.2.4 Investments in Angel Funds

1. Angel Funds can be raised by issuing units to angel investor.
2. Minimum requirement of the corpus is Rs. 2 crores for angel fund.
3. An angel investor should invest at least Rs. 25 lakhs.
4. Angel fund shall raise funds through issue of private placement by issue of placement memorandum.

Scheme

Up to 200 investors should be allowed for the scheme of Angel Funds.

Investment by Angel Funds

1. Angel fund shall invest in venture capital undertakings having turnover of less than Rs.25 crore, are not sponsored, promoted or related to an individual group

whose group turnover exceeds Rs.300 crore and are not companies with family connection who are investing in the company.

2. According to regulations with amendment, "Investment by angel fund shall not be less than Rs. 25 lakh and not more than Rs. 5 crore".
3. Funds shall not invest in associates.
4. Shall not invest more than 25 per cent of the total investment under all its schemes in one venture capital undertaking.

Check your progress-2.

A) Select the appropriate alternative from among given below each statement

i) Angel funds can be raised by issuing ----- to angel investor.

a) Gold Bond b) Units c) Postal certificate d) Silver bond

ii) Up to ----- angel investors should be allowed for the scheme of angel fund.

a) 200 b) 150 c) 250 d) 300

iii) Investment by angel fund shall not be less than -----.

a) Rs. 50 lakh b) Rs. 25 lakh c) Rs. 10 lakh d) Rs. 20 lakh

iv) SEBI (Alternative Investment Funds) Regulations, 2012 came into force by notification in official Gazettee on -----.

a) 21 June, 2012 b) 21, May, 2012 c) 21 January, 2012 d) 21 March, 2012

v) An Angel fund shall have a corpus of at least ________ rupees.

a) 5 corer b) 15 corer c) 7 corer d) 10 corer

vi) The word 'Angel Investor' was used in 1978 by __________ who was professor at the university of New Hampshire.

a) Jan T. Gross b) Cass R. Sunstein
c) William Wetzel d) Anthony Grafton

B) State True or False.

1. Already registered Alternative Investment Funds may apply for conversion of it into an angel fund.
2. An angel investor should invest at least Rs. 25 lakhs.
3. Investment by angel fund shall not be more than Rs. 5 Crore.
4. The term 'Angel' was used in 1878 for the first time.
5. Upto 400 investors should be allowed for the scheme of Angel fund.

4.2.3 Financial Technology (FinTech)

Financial technology (better known as fintech) is used to describe new technology that seeks to improve and automate the delivery and use of financial services. At its core, fintech is utilized to help companies, business owners, and consumers better manage their financial operations, processes, and lives. It is composed of specialized software and algorithms that are used on computers and smartphones. Fintech, the word, is a shortened combination of "financial technology." When fintech emerged in the 21st century, the term was initially applied to the technology employed at the backend systems of established financial institutions, such as banks. From 2018 or so to 2022, there was a shift to consumer-oriented services. Fintech now includes different sectors and industries such as education, retail banking, fundraising and nonprofit, and investment management, to name a few. Fintech also includes the development and use of cryptocurrencies, such as Bitcoin. While that segment of fintech may see the most headlines, the big money still lies in the traditional global banking industry and its multitrillion-dollar market capitalization.

Broadly, the term "financial technology" can apply to any innovation in how people transact business, from the invention of digital money to double-entry bookkeeping. Since the internet revolution, financial technology has grown explosively. You likely use some element of fintech on a daily basis. Some examples include transferring money from your debit account to your checking account via your iPhone, sending money to a friend through Venmo, or managing investments through an online broker. According to EY's 2019 Global FinTech Adoption Index, two-thirds of consumers utilize at least two or more fintech services, and those consumers are increasingly aware of fintech as a part of their daily lives.

As per the State of Indian Fintech Report Q2, 2022, the Indian fintech market is one of the fastest-growing globally, estimated to reach $1.3 trillion by 2025, growing at a CAGR of 31%. Presently more than 2000 fintech companies are in operation in India. The use of ABCD (Artificial Intelligence, Blockchain, cloud computing and Big Data) and various other technologies in order to render financial services may be seen as the basic driver of Fintech. Some examples of fintech applications include roboadvisors, payments apps, P2P lending apps, investment apps, crypto app and many more.

Global Fintech Landscape as on 2021 (Source – www.info.currencyfair.com)

4.2.3.1 Meaning:

The 21st century has seen the rise of many new innovative ideas and some of the best uses in technology. One of them is 'Financial Technology', also popularly known as 'Fintech'. Today, more than 26000 fintech companies exist globally and the number is expected to increase. Fintech companies are those companies which deliver financial services such as borrowing as well as lending money by using technology such as machine learning, artificial intelligence, Big Data etc

The term financial technology, which is better known as fintech is used to describe new technology that seeks to improve and automate the delivery and use of financial services. At its core, fintech is utilized to help companies, business owners, and consumers better manage their financial operations, processes, and lives. It is composed of specialized software and algorithms that are used on computers and smartphones. Fintech, the word, is a shortened combination of "financial technology."

The term 'Fintech' is a short combination of "financial technology." It's a catch-all term for technology used to augment, streamline, digitize or disrupt traditional financial services.

Fintech refers to software, algorithms and applications for both desktop and mobile. In some cases, it includes hardware, too-like internet-connected piggy banks. Fintech platforms enable run-of-the-mill tasks like depositing checks, moving money between accounts, paying bills or applying for financial aid. They also facilitate technically intricate concepts, including peer-to-peer lending and crypto exchanges. Hence, it is stated that the entry of fintech companies has disrupted the traditional/conventional means of banking. This has given rise to alternative finance and a certain amount of business being taken away from banks by such firms. Traditional banks are often seen to face the following issues –

1. **Highly regulated –** Traditional banks are bound to complex and time consuming procedures.
2. **High operational costs** due to a large network of branches and manpower involved in traditional banking system.
3. **Mostly risk** averse and hence do not look beyond the traditional way of doing Low
4. **Low Investment** in new ideas and technological innovations

However, considering the ever changing landscape of the banking industry, banks may consider the following to overcome competition from fintech firms –

Investment in Technology – Understanding the role of technology in banking and a focussed approach in utilisation of the budget for digital transformation for creation of better products and services. This may also include creating more payment options to customers, improving TAT by leveraging on technology for assessment of loan, simplifying procedures various internal procedures for customers etc

Integrate fintech ideas – Fintech aims at innovation and disruptive technology while banks have a large customer base which is possible to connect and create demand. Banks should leverage the technology and opportunities o-ered by fintech firms for their advantage. This can help banks understand their customer and the market better and also provide the best financial solutions possible.

Collaboration – There are many areas and opportunities which are yet to be tapped by banks. Banks should explore all possible venues including options to mechanise and improvise the internal processes through a way of collaboration with the fintech companies to ensure better eciency and utilisation of resources. This would help banks to save time and resources in order to cope up with the technological innovations done by the Fintech firms.

It seems that the growing technology and awareness, customers are always looking for new and innovative ways to get things done in an easy, fast and convenient manner. Fintech firms and banks have their own Unique Selling Propositions (USPs) and in days to come, we may see more novel ways of doing banking.

4.2.3.2 Application of Fin-Tech to different areas of finance:

FinTech can be applicable to different areas of finance and which are broadly listed as under

1. **Application of FinTech for Borrowers and Lenders:** Borrowing and lending is one of the important area where fintech is playing an important role. Individuals can borrow money from other individuals. This type of lending is generally known as peer to peer lending ie.P2P lending. When a person or group of persons lend money to a business it is called as peer to business lending or P2B lending. With this method investors can obtain can obtain higher returns and the companies can get money by deducting charges from the repayment of buyers.

For example Funding Circle, which provide online platform for borrowers and lenders.

2. **Application of FinTech as Gateway for Payments:** Payment Gateway provides online platform to customers to pay directly to retailer’s website for goods or service. Now a day’s credit cards, debit cards and digital wallets etc. are available for making payments. These different payment ways are merged by FinTech firms into handy applications. Online seller can incorporate these handy applications to their websites. The charges for handling these transactions are high in Banks. FinTech companies combine all these payment methods and offer the service by eliminating costs.

For example The companies which sell their products or offer services directly to customers widely use payment gateway applications like Stripe, Alipay.

3. **Application of FinTech for Digital Wallets:** Digital wallet can be used as payment method. The user loads certain amount of digital currencies into their wallets and uses this virtual money for making payment to those companies who accept payment through digital wallets. The companies offering this technology charges minimum amount to users.

4. **Application of FinTech for E-commerce:** The licensed bank provides this service to their clients. The clients make purchases without paying interest for their buying. Low-fee-installments are made available to the clients for their purchases. The purchase transaction is split in such a manner that the consumer can pay installments for their purchased product.

For example Klarna, offers payment processing for online shopping. Pay-post-delivery, payments for web stores etc are the payment methods offered by Klarna.

Application of FinTech for Stock Trading: The broker and investor can make online conversation on digital platforms. Majority of traditional investment platforms charges high fees though there is no need of actual financial resources in these transactions. Many businesses adopting FinTech created fee-free platforms and encouraged the investors to trade freely through their phones.

For example due to Robinhood application for digital stock trading customer can make commission free trading along with trading in exchange-traded funds.

5. **Insurtech:** Application of fintech to industrial sector is increasing. It includes application of technology such as data analytics, artificial intelligence, machine learning to improve the working of insurance industry. Due to fintech underwriting process became fully automated. In many insurance companies algorithms powered by artificial intelligence has increased the speed of approval process of application and helps the customers to complete the process faster. Insurtech is appealing the youth. Various insurtech companies are providing facilities to their customers for filing online claims through their mobiles. Thus due to insurtech the process from filling application to settlement of insurance claim, are fully digital and transparent.

6. **Application of Fintech for Investment Management:** Investment management is one of the important area of finance where fintech is playing important role. In India, majority of people are interested in traditional avenues of investment like gold, real estate etc. Fintech has provide them opportunities to invest in financial assets like mutual funds, stocks or exchange- traded funds. Fintech make use of Big Data, Artificial Intelligence, Machine learning to evaluate investment opportunites, optimize portfolio.

For example 'Robo-adviser' assist investors in making investments at lower cost and with greater ease of access.

7. **Application of Fintech for Wealth Management:** Wealth Management deals with the assets and liabilities of the client. Wealth management helps the client to plan the client for their financial future according to the set goals. In fintech wealth management, the technology of robo advisors, portfolio management software, digital communication channels is used. Fintech is playing an important role in digital economy of India. With innovative technologies, fintech is applied in almost all areas of finance and offering better financial services to customers who need it. It is one of the fastest growing sector in Indian economy. In India many companies are making use of fintech due to newer and innovative technologies and handy applications.

4.2.3.3 Fintech companies in India

India has the second-largest base of internet users1 and this has had a direct impact on the demand for digitised financial services. In fact, India emerged as a global fintech power and ranked third in the world in terms of total fintech companies (as of 2023). Herewith, we will tried to enlisted the welknown fintech companies in India. Fintech, as the name suggests, is the amalgamation of finance and technology. A lot of players in the market are using technology to simplify financial services such as lending, insurance, investment, trading, and budgeting among others. As the fintech ecosystem expands, many players are focusing on niche sectors. Needless to say, the development has been nothing short of rapid. India is home not only to one of the oldest and richest cultures in the world, but also to the best fintech solutions. According to the recently released Indian Fintech Report, India is now the world's second-largest fintech ecosystem after the United States.

Moreover, in 2019, Indian FinTechs surpassed Chinese FinTechs in raising funds for the first time.

However, Indian FinTechs has come long. Statistics show that India has a more than 10-year head start in the FinTech space. India's FinTech industry is growing fast. The entire world's major financial institutions, leading financial technology and services companies, and major financial services groups are setting up their offices in India. Silicon Valley fintech startups are also tracing out their roots to India, and many of them are launching their Blockchain DeFi offerings in India. With a strong foundation in the current technology trends, and having matured in the area of regulation, India offers a wide range of opportunities for FinTechs.

- **Factors that boosted the growth of Fin-Tech companies in India**

1. **Growing competition –** Globalisation has opened doors to new opportunities and more demanding customers. Banks and financial service providers are looking for better and novel ways to engage the customer and deepen their relationship. At this point, retention of a customer is seen as a crucial part doing business in order to sustain the growth in competition. In such a scenario, FinTech services have been considered as a game changer to serve the customer better and sustain competition and have led many banks in search of suitable fintech firms for collaboration.

2. **Availability of data –** Data regarding spending habits, loan details, credit worthiness, banking services availed, insurance details, demographics (age, gender etc) and much more is now being recorded by various companies and provided as per demand. Fin-tech companies require such data to design custom made product packages and such data is now easily available.

3. **Penetration of smart phones and internet enabled devices –** India has one of the highest technology adoption rates in the world. The transition into smartphones and other internet enabled devices has helped banks and financial service providers to connect with the customers like never before. Since the services provided by Fintech companies mostly require internet support, this has also been a key advantage for fintech companies who are looking to connect with a large group of customers.

4. **Robust market –** Unlike the conventional bank and financial service providers, fintech companies have been able to provide loans even to persons with no past record of availing loans. This information is primary to assess the credibility of the borrower. Using new age technology, fintech companies have been able to assess the credit worthiness of the borrowers even if they have no loan history. This paves way to the access the opportunities of a new and robust market which was not very well tapped before.

5. **Government support –** The government of India has been in support of the growth of the fintech ecosystem. The launch of the 'Open Credit Enablement Network and Account Aggregator framework' by the government has helped to improve the way loans are availed. Government support has also been been vital to transition into a paperless and cashless system which is now being adopted by several banks and NBFCs. Moreover, strong policies to protect the rights of the customers and their data is ensured by the government which has helped to build the public trust and confidence over the Fintech business.

Types of Fintech Companies
(Source: https://enterslice.com/)

Top Fintech Companies in India

Paytm	Lendingkart	MoneyTap	Instamojo
Razorpay	Shiksha Finance	Pine Labs	Zest Money
PolicyBazaar	InCred		

(Sources: https://enterslice.com/)

Here, tried to cover some of the Top Fintech Companies in India. Hopefully, the information will help many to select the best-suited alternative among the plethora of choices! Leading fintech companies in India include Paytm, Lendingkart, MoneyTap, Instamojo, Razorpay, Shiksha Finance, Pine Labs, ZestMoney, PolicyBazaar, and InCred. FinTech companies in India are greatly helping the under-served society with their services and are also performing well for India being the most potent market in the world! Slightly over 50% of the Indian populace is now an internet user. Our average data consumption per month is 20 GB, which is expected to rise to around 47 GB/month in 2027. Reports also reveal that Indian mobile data consumption is now more than the USA & China combined. Moreover, Nokia's annual MBIT report revealed that in 2022, 70 million 5G devices were shipped to India, and the roll-out of 5G services will enhance the data usage numbers by leaps & bounds. The internet-dominated society will seek more digitized financial services, and the top FinTech companies in India are leaving no stone unturned in enhancing their service spectrum with each passing day. As India is the second largest internet-user base, in commensuration with the numbers, India is also the second largest FinTech hub in the world! Including 25 unicorns, around 2200 FinTech companies are operating in India, and $1/5^{th}$ of them are in the payment sector alone. Hence, here enlighten on the some leading FinTech company in India.

1. Perfios

With a vision to develop an ecosystem where financial decisions are backed by real-time data, Perfios has established itself as the biggest SaaS B2B FinTech organization. Leveraging the power of Artificial Intelligence & ML algorithms, Perfios is empowering global financial institutions to make better- informed decisions. Here, a strong team of the world's best brains of the domain craft state-of-the-art Al-powered digital solutions, and this has garnered them the trust of more than 900 banks and Fls. Perfios specializes in real-time insurance claim and credit decisions, real-time fraud control, insurance underwriting solutions, onboarding KYC automation, litigation automation, Al-powered cognitive, fraud checks, and other solutions. With such expertise, Perfios is helping other FinTech companies in India in their day-to-day operations.

2. PayTm

Paytm is an Indian multinational financial technology company, that specializes in digital payments and financial services, based in Noida. It was founded in 2010 by Vijay Shekhar Sharma under One97 Communications. Fintech has the potential to transform other financial services like insurance, investment, remittances. However, regulation must help, not hinder its evolution. The acronym of Pay through Mobile, PayTm is one of the pioneer and most popular payment FinTech Companies in India. It provides consumers with payment, banking, lending, and even insurance services! Though initially, they provided the financial services through their wallet only, but later developed into UPI payments as well. Now PayTm processes more than 5 million transactions daily and is a key player in the digital economy. PayTM has 450 million registered users and 60 million bank accounts under its PayTM bank. In times of demonetization, PayTM added a record 20 million users. Approval by RBI greatly enhances PayTM's credibility, which is already the most popular mobile wallet & UPI app in India.

3. LendingKart

LendingKart is a top FinTech company in India with its major offering in lending money- as its name suggests! The digital lending services of LendingKart can be broadly compartmentalized into four sections, viz. Business Loans, Working Capital Loans, MSME, SME loans, and special business loans for Women. While the market is callously competitive, LendingKart, with its competitive edges, has successfully established itself in India. The best part is online approval and quick sanctioning. Following the document verification, which is an easy and smooth process here, loans can be disbursed within 3-4 working days. Moreover, loans are collateral-free here, with highly flexible repayment options. While there is no hidden cost, the interests are also lenient.

4. Zerodha

When asked to tell about some top FinTech companies in India operating in the wealth management division, Zerodha's name would top the list. It is an online platform for investing in stocks, mutual funds, and others- all in one place. The best part is commission-free mutual funds, which can be delivered straight into the Demat account. This intuitive platform streamlines market data and presents it in the form of easy-to-understand charts. Being registered with SEBI and CSDL, Zerodha is a completely legitimate platform. On this platform, one can easily choose multiple financial tools like stocks, IPOs, Gift Stocks, mutual funds, government securities, sovereign gold bonds, and others to invest in.

5. DMI Finance

An older player among the FinTech companies in India, DMI Finances was established in 2008 with an outlook to transform credit transfer in India. And now, it is one of the top FinTech companies in India, operating as a NBFC company. With completely digital underwritings & loan management, they particularly work with the FinTech organizations in the B2B divisions. Their major offerings include business loans, housing finance, and asset management services. DMI Finance is a registered NBFC under the 1965 Companies Act of India and is regulated by RBI, and these facts bolster its candidature for those looking for lending services by top FinTech companies in India.

6. Satya Microcapital

Smaller shops and vendors, in most cases, are out of loan eligibility criteria; this bottom-of-the- pyramid section is, therefore, primarily underserved. To assist them in raising capital and empowering them monetarily and societally, Satya Microcapital, one of the leading Fintech companies in India, is providing lending facilities online. The Delhi-based NBFC firm is on a mission to catalyze the socio-economic development of low-income entrepreneurs. Major offerings include

- **Limited Liability Loans:** In this, a group of people can take a loan combined, and each member is equally liable for the repayment.
- **Micro Business Loan:** These special unsecured loans are for the MSME segments- the backbone of the Indian Economy and the driving force behind the outlook of self-reliant India.
- **Consumer Durable Loan:** These small amount loans are to help consumers purchase durable household goods. The hassle-free payback options with flexible & affordable EMIs make them a popular choice among the masses.
- **Individual Micro Loans:** these are a kind of personal loan, disbursed for any necessity or financial emergency.

7. PhonePe

PhonePe is one of the most renowned FinTech companies in India, with over 440 million users! Headquartered in Bengaluru, A digital payments and financial services company, PhonePe offerings are availed through a UPI-based app that went live in 2016. With this app, available in 11 Indian languages, the users can send/receive money, recharge services, pay utility bills, invest in funds, buy insurance products, and even digital gold. PhonePe is licensed by RBI for the issuance and operation of a semi-closed Prepaid Payment system, and mobile transactions with its services are secured by Cloudflare. From 2018 to 2022, PhonePe has won several awards and recognitions for its innovative services. Now PhonePe has incorporated the Account Aggregator system in its framework, and this will help customers in availing loan services with much ease and pace.

8. Acko

Acko is operating in the insurance division but is primarily for motor insurance. They also offer advice and loans for getting the right vehicle. Their comprehensive resource guide has helped numerous individuals get the right product. Acko has revolutionized the car insurance concept with its digital-only model. With Acko, one can easily purchase an insurance plan without the involvement of any third-party medium. Other special benefits include Financial Protection against medical emergencies, No room rent capping, No deduction on claim amount, and several other additional coverages. Personalized offerings for different use cases are also the competitive edges at Acko.

9. Unnati

Unnati is a top-notch Agri-Fintech organization. Empowering farmers through digital technologies, Unnati is bringing efficiency to farming practices. Leveraging advanced techniques and offering transparency in the farming business, Unnati is also lessening the losses to the farmers, as unpredictability is the biggest threat in this business. Unnati not just offers the right advice for every crop and land and weather but also supports farmers at every step of the crop lifecycle. Other important offerings include:

1. Financing
2. Insights for better yield

3. Correct Advisory

4. Providing buyer's information and platform for better deals

10. Upstox

One of the newbies among FinTech companies in India, Upstox is also an online investment platform. Here the equity delivery, account opening, and 3-in-1 account everything comes for free, and the per- trade cost is also less. With this low-cost broker platform, one can save a huge amount of money with Upstox. Upstox's transparency and highly affordable fees make it a popular choice among investors of all domains and dimensions. This platform is perfectly apt for long-term investing and intraday investments as well. IPO applications and mutual fund investments are very easy here, so beginners can easily give it a try. All these features have made Upstox a unicorn in the FinTech division.

In brief it is stated that, with the advancements in digital technologies i.e. FinTech services are on the rise, and in India, the FinTech adoption rate is 87%, which is significantly higher than the global average rate of 64%. In 2021, the FinTech Market size was about $50 Billion, which is estimated to rise to $150 Billion by 2025. India Stack, Technical Innovations, Internet & Smartphone Penetration, Favorable Demographics, and Financial Inclusion initiatives are the main growth drivers of the FinTech division, and with these factors, we are hopefully going to witness much more favorable disruptions in the market. Fintech is now so pervasive in financial services that it's all but ubiquitous. Consumers, businesses and all sorts of financial services firms are increasingly turning to imaginative combinations of software, hardware and data to create and deliver both new and traditional financial products and services. Fintech is firmly entangled in the fabric of our financial society, and it appears its influence will only grow in the future.

Check Your Progress-3

A. Select the appropriate alternative:

i) A ------ is a term that utilizes technology to change, improve and automate the delivery of financial services.

a) Startups b) Financial Technology

c) Angel Funds d) Private Equity

ii) Fintech helps ------ in better management of their financial operations, processes and lives.

a) Companies b) Consumers c) Business owners d) All of the above

iii) Application of FinTech to different areas of finance includes ……..

a) Application of FinTech to Stock Trading

b) Application of FinTech to E-commerce

c) Application to Investment Management

d) All of the above

iv) Which is of the following is an example of a digital financial tool……

a) Cash b) Credit Card c) Cheque d) Demand Draft

v) FinTech companies in India includes ....

a) Paytm b) Unnati c) Acko d) All of the above

B) State True or False.

1. FinTech companies do not make use technology for their business.
2. Insurtech means application of technology to insurance sector.
3. When a person or group of persons lend money to a business it is called as peer to business lending or P2B lending.
4. Finacial technology is not useful for consumers.
5. Robinhood make it easy to buy and sell stocks, exchange-traded funds.

4.3 Summary

Startup India scheme was launched in 2016, aims to assist ambitious, zealous entrepreneurs. Entrepreneurs face numerous problems at every stage of growth of enterprise. Startups are in need for sustained funding access, expertise assistance throughout various stage. Newly started startup need money at every walk. In 2015, SEBI has opened the door and simplified the process of fund raising for startups. Startups has allowed to raise funds from public through initial public offer. SEBI has laid down regulations on startup listing and fund raising. To give support and promote startup India Government of India initiated various schemes. These schemes provide financial, regulatory and infrastructural support to startups in every sector at every stage. AIM, Startup India Seed Fund Scheme, Startup India Initiative etc. are providing financial assistance for new startups.

There are various sources of finance available for startups. Venture capital is a type of financing having exclusive growth potential in long period. Private equity is a type of financing in which investors buys a stake in private company with a hope of increase in the value of their stake. Venture capital is subset of private equity. Angel funds are high net worth investments. Angel funding may be on time investment or it may be ongoing support. The term angel investor was used to money providers first in 1978 by William Wetzel. SEBI has laid down regulations regarding angel funding. It includes definition, registration, investments in angel funds, schemes, investment by angel fund. In this unit we learn the concept of FinTech and it present status in India. Fintech is firmly entangled in the fabric of our financial society, and it appears its influence will only grow in the future.

4.4 Terms to Remember

- **Venture Capital -** Provides funding to new companies or ventures with limited operating history but having exceptional growth potential in long term.
- **Private Equity –** Private equity is a method of financing in which investor buys a stake in a private company with a goal of selling the stake at added value.
- **Angel Fund –** Angel funds are the funds where the money is pooled by private wealthy investors known as angel investors, for investing in startups.
- **FinTech** - FinTech is a term used for mentioning use of software, mobile applications and other technologies like artificial intelligence, machine learning for improving and automation of traditional forms of finance to individual or business.

4.5 Answers to check your progress

➢ **Check Your Progress-1**

A) i) Ans – a ii) Ans – c iii) Ans – b iv) Ans – a v) Ans – d

B) i) Faise ii) True iii) True iv) False v) True

➢ **Check Your Progress-2**

A) Ans – b ii) Ans – a iii) Ans – c iv) Ans – b v) Ans – d vi) Ans - c

B) i) True ii) True iii) True iv) False v) False

- **Check Your Progress-3**

A) i) Ans – b ii) Ans – d iii) Ans – d iv) Ans – b v) Ans – d

B) i) False ii) True iii) True iv) False v) True

4.6 Exercise:

A. Long type questions

1 Explain various Government schemes available for new startups in the form of finances.

2 Give SEBI Regulations on startup listing and fund raising.

3 Differentiate between venture capital and private equity.

4 What do you mean by FinTech? Explain the application of FinTech to different areas of finance.

5 Which are the FinTech companies in India?

B. Short type questions

a. Write fund raising norms for startups.

b. Explain SEBI Regulations on startup listing.

c. State origin of angel funding.

d. Give SEBI regulations on angel funding

e. Write application of FinTech to different areas of finance.

f. What do you mean by FinTech.

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