INDIAN FINANCIAL SYSTEM

Introduction

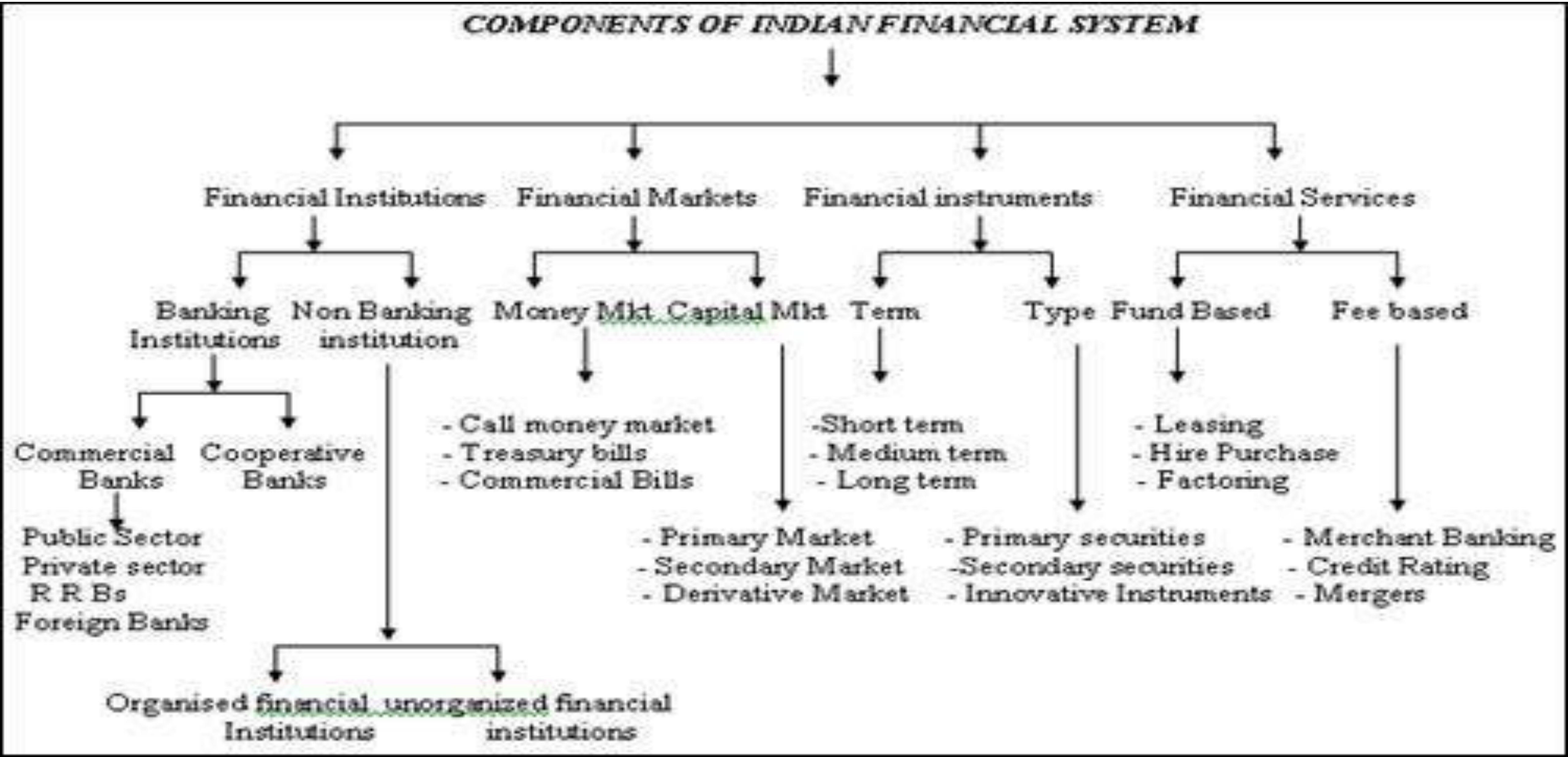
- The economic development of any country depends upon the existence of a well organized financial system

- It is the financial system which supplies the necessary financial inputs for the production of goods and services which in turn promote the well being and standard of living of the people of a country

- The financial system acts as a connecting link between savers of money and users of money and thereby promotes faster economic and industrial growth.

- Thus financial system may be defined as “a set of markets and institutions to facilitate the exchange of assets and risks.”

Indian Financial System



1. FINANCIAL INSTITUTIONS

- A financial institution is an establishment that conducts financial transactions such as investments, loans and deposits.

  A financial institution (FI) is a company engaged in the business of dealing with financial and monetary transactions, such as deposits, loans, investments and currency exchange.

  A financial institution is an intermediary between consumers and the capital or the debt markets providing banking and investment services.

Banking Institutions

- A **bank** is a financial institution that accepts deposits from the public and creates credit.

Banking Regulation Act of India, 1949 defines Banking as

"accepting, for the purpose of lending or of investment of deposits of money from the public, repayable on demand or otherwise or withdrawable by cheque, draft order or otherwise."

Commercial Banks

- A **commercial bank** is an institution that provides services such as accepting deposits, providing business loans, and offering basic investment products.

- Commercial Banks may be

- Public Banks
- Private Banks
- Regional Rural Banks
- Foreign Banks

REGIONAL RURAL BANKS

- Kerala Gramin Bank
- Allahabad UP Gramin Bank
- Andhra Pradesh Grameena Vikas Bank
- Andhra Pragathi Grameena Bank
- Arunachal Pradesh Rural Bank
- Gramin Bank of Aryavart
- Assam Gramin Vikash Bank
- Baitarani Gramya Bank
- Bangiya Gramin Vikash Bank
- Baroda Gujarat Gramin Bank

FOREIGN BANKS

- ABN-AMRO Bank – THE ROYAL BANK OF SCOTLAND
- Abu Dhabi Commercial Bank
- American Express Bank Ltd.
- Barclays Bank
- BNP Paribas
- Citibank
- DBS Bank Ltd
- Deutsche Bank
- HSBC Ltd
- Standard Chartered Bank
- State Bank of Mauritius Ltd

Co-operative Bank

- They are registered under the Cooperative Societies Act, 1912.
- They are regulated by the Reserve Bank of India under the Banking Regulation Act, 1949 and Banking Laws (Application to Cooperative Societies) Act, 1965.

Non Banking financial Institutions

- A non-bank financial institution (NBFI) or non-bank financial company (NBFC) is a financial institution that does not have a full banking license or is not supervised by a national or international banking regulatory agency.

2. FINANCIAL MARKETS

- There is no specific location to indicate a financial market.
- Wherever a financial transaction take place, it is deemed to have taken place in the financial market.
- Financial Markets can be referred to as those centers and arrangements which facilitate buying and selling of financial assets, claims and services.

Money Market

- Money Market is a market for short term loans or financial assets
- It is a market for the lending and borrowing of short term funds
- Trading is done on a rate known as discount rate which is determined by the market and guided by the availability of and demand for the cash in the day to day trading.
- Money market deals with near substitutes for money like trade bills, promissory notes and government papers drawn for a short period not exceeding one year

Call Money Market

- The call money market refers to the market extremely short period loans, say one day to fourteen days.
- The loans are given to brokers and dealers in stock exchanges and similarly banks with sufficient funds lend to other banks with deficit funds in the call money market
- Borrowers and lenders in a call money market contact each other over telephone. Hence it is basically a over-the-telephone market
- After negotiation over the phone, the borrowers and lenders arrive at a deal specifying the amount of loan and rate of interest.

- Commercial Banks can quickly borrow from the call money market to meet their statutory requirements
- They can also maximize their profits easily by investing their surplus funds in the call market during the period when call rates are high

Commercial Bills market or Discount Market

- A commercial bill is one which arises out of genuine trade transaction, i.e., credit transaction.
- As soon as goods are sold on credit, the seller draws a bill on the buyer for the amount due.
- The buyer accepts it immediately agreeing to pay the amount mentioned there in after a certain specified date.
- Thus, a bill of exchange contains a written order from the creditor to the debtor, to pay a certain sum, to a certain person, after a certain period.
- It is drawn always for a short period ranging between 3 months and 6 months

TREASURY BILL MARKET

- Just like commercial bills which represent commercial debt, treasury bills represent short term borrowings of the Government.

- Treasury bill market refers to the market where treasury bills are bought and sold.

- Treasury bills are very popular and enjoy a higher degree of liquidity since they are issued by the Government

- A TB is nothing but a promissory note issued by the Government (RBI) under discount for a specified period stated therein
- The Govt. promises to pay the specified amount mentioned therein to the bearer of the instrument on the due date.
- The period does not exceed one year.
- It is purely a finance bill since it is does not arise out of any trade transaction.
- The treasury bill rate is fixed by the RBI from time to time.

Types of TB

- 91 days TBs
- 182 days TBs
- 364 Days TBs

Certificate of deposit

- These are negotiable, unsecured instruments presented in the bearer form.
- .these instruments are issued by commercial banks and financial institutions.
- Maturity periods of these instruments range from 91 days to 1 year.

Commercial paper

- Commercial paper is an unsecured money market instrument issued in the form of promissory note.
- Negotiable and transferable.
- It has a maturity period ranging from a minimum of 15 days to maximum of one year.
- These are primarily period ranging from a minimum of 15 days to a maximum of one year.

Capital Market

- A capital market is a financial market in which long-term debt or equity-backed securities are bought and sold
- Capital market is a market where buyers and sellers engage in trade of financial securities like bonds, stocks, etc.

Primary Market / New Issue Market

- The new issue market deals with the new securities which were not previously available to the investing public
- The securities that are offered for the first time
- The market therefore makes available a new block of securities for public subscription
- It is for raising fresh capital for the company
- The instruments are equity shares, preference shares ,debentures, right issues, deposits etc

Secondary Market/Stock Exchange

- The stock exchange is a market for old securities
- Those which have been already issued and listed on a stock exchange
- These securities are purchased and sold continually among investor without the involvement of companies

- Market where long-term securities are voluntarily exchanged at competitive prices determined according to free play of demand and supply.
- SE is a recognized and formal association of members for buying, selling or dealing in securities under a set of accepted market rules and regulations.
- **SEBI(Securities and exchange board of India**) is the regulatory authority of stock exchanges in India.

Major objectives of SEBI

- Regulation
- Protection
- Prevention
- Code of conduct

Functions of SEBI

1.Regulatory functions

- Registration
- Regulating work
- Levying fee
- Regulation by legislation

2.Development functions

- Training
- Research
- Flexible approach

3.Protective function

- Prohibition
- Checks on insider trading
- Protection and promotion

Functions of stock exchange

- Provides liquidity and marketability
- Determination of prices
- Fair and safe market
- Facilitates economic growth
- Spreading of equity cult
- Scope of speculation

STOCK EXCHANGES OF INDIA

2 National Stock Exchanges and 14 Regional Stock Exchanges

- **Bombay Stock Exchange Ltd**
- **National Stock Exchange**
- Bangalore Stock Exchange
- The Ahmedabad Stock Exchange
- Bhubaneswar Stock Exchange
- Calcutta Stock Exchange
- Cochin Stock Exchange
- The Delhi Stock Exchange
- The Gauhati Stock Exchange
- Jaipur Stock Exchange
- The Ludhiana Stock Exchange
- Madhya Pradesh Stock Exchange
- Madras Stock Exchange
- Pune Stock Exchange
- U P Stock Exchange
- The Vadodara Stock Exchange

BASIS OF DIFFERENCE	CAPITAL MARKET	MONEY MARKET
time span	long term and medium term securities	maturity period of a maximum one year
liquidity	less liquid	highly liquid
returns expected	higher possibility of gains	Return is lower
instruments	equity shares, preference shares, bonds and debentures	commercial papers, treasury bills and certificates of deposit
risk	Risky as regard to both return and principal repayment	Safe as securities traded for short duration

3. FINANCIAL INSTRUMENT

- Financial Instruments refers to those documents which represent financial claims on assets

- Financial instruments are also called financial securities

Term Based Financial Instruments

- ***Short Term Securities:-***
  - Short term securities are those which mature within a period of one year.
  - E.g. BOE, TB, etc.
- ***Medium Term Securities:-***
  - Medium Term Securities are those which have a maturity period ranging between one to five years
  - E.g. Debentures maturing within a period of five years
- ***Long Term Securities:-***
  - Long Term Securities are those which have a maturity period of more than five years
  - E.g. Government Bonds maturing after ten years

Type Based Financial Instruments

- **Primary Securities or Direct Securities**
  - These are securities directly issued by the ultimate investors to the ultimate savers.
  - E.g.; shares and debentures issued directly to the public

- **Secondary Securities or Indirect Securities**
  - These are securities issued by some intermediaries called financial intermediaries to the ultimate savers.
  - E.g.; UTI and mutual funds issues securities in the form of units to the public and the money pooled is invested in companies
  - These securities are again classified into;
    - Short term securities
    - Medium term securities
    - Long term Securities

4. FINANCIAL SERVICES

- **Financial Services** is a term used to refer to the services provided by the finance market.

- **Financial services** are the economic services provided by the finance industry, which encompasses a broad range of businesses that manage money, including, banks, credit card companies, insurance companies, accountancy companies, consumer-finance companies, stock brokerages, investment funds, individual managers and some government-sponsored enterprises

TYPES OF FINANCIAL SERVICES

- **Fee based financial services** charge a fee to the person using their services.

- E.g..
  - Merchant Banking
  - Credit rating
  - Mergers etc.

- **Fund based financial services** retained a certain portion of the equities purchased.

- Eg.
  - Leasing
  - Hire Purchase

Role of Indian Financial System

1. Pooling of Funds,
2. Capital Formation,
3. Facilitates Payment,
4. Provides Liquidity,
5. Short and Long Term Needs,
6. Risk Function,
7. Better Decisions,
8. Finances Government Needs,
9. Economic Development.

Weaknesses of Indian Financial System

- Lack of Co-ordination between different financial institutions
- Monopolistic Market Structure
- Dominance of Development Banks in Industrial Financing
- Inactive and erratic capital market
- Imprudent financial practice

THANK YOU