Capital Market in Professional Perspective: An Overview

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Capital Market is a broad concept, however, before understanding the Capital Markets in India, one has to consider the broader framework of Financial Market of which Capital Market is a part and even before that one shall dwell upon the even broader term 'market'. A market can be defined in a common man's language as a place where two parties can gather to facilitate the exchange of goods and services. Financial Market just like an ordinary market acts as a platform where two parties meet to exchange money or instruments which are convertible into money. It acts as a link between two different groups, one who invest money or lends i.e. having surplus money and the other, who borrows i.e. having deficit money. It facilitates this function by acting as an intermediary between the borrowers and lenders of money or sellers and buyers of instruments. Read on to know more…

The market consists of various players. On the lender or investor side consists of investors such as individual investors, angel investors, venture capitalists, banks and other financial institutions (FI), etc. whereas the borrower or user side consists of any person who is in need of money. There are various laws in India to regulate the players dealing in financial instruments and have been drafted by regulators to protect the interest of both the investors as well as the borrowers. The intermediaries who act as middleman are also governed by such laws for trading the various financial assets and instruments.

Financial Markets can be broadly categorised as consists of two major segments:
(a) Money Market; and
(b) Capital Market.

While the money market deals in short-term credit, the capital market handles the medium term and long-term credit. The capital market can also be further classified in two broad categories (i) Securities Market and (ii) Other Forms of Lending.

Let us discuss the money market in brief and capital market in detail.

1. MONEY MARKET

The money market refers to the market where borrowers seek short-term funds from lenders to solve their liquidity needs quickly, adequately and at reasonable cost. Money market instruments are generally financial claims that have very low default risk, maturities under one year and high marketability. Money market is closely regulated. The institutions involved include RBI, Commercial banks, Non Banking Financial Institutions, etc. The different money market instruments issued include: -

a. **Call Money, Notice Money or Term Money**[1]: In the money market, scheduled commercial banks, co-operative banks and primary dealers borrow and lend funds to each other on unsecured basis to tide over daily liquidity mismatches. If the period is overnight, it is called "Call Money". If the period is more than 1 day and up to 14 days it is called "Notice Money". Money lent for 15 days to 1 year is called "Term Money". Interest rates are decided among participants depending upon general liquidity conditions and availability of funds among participants.

b. **Treasury Bills**[2]: They are issued by the Central Government to finance the short-term requirements of the Government of India and are the safest money market instruments. T-Bills are issued through bidding process (auctions) on electronic platform called the E-Kuber and are issued at present for 91 days or 182 days or 364 days. Cash Management Bills (CMB's) similar to T-Bills are issued for less than 91 days. T-Bills are most liquid, highly traded zero coupon bonds issued without any periodic coupon payments. The return to the investors is the difference between the maturity value or the face value and the issue price.

c. **Certificate of Deposits**[3]: They are issued by the banks or Financial Institutions as per the guidelines of RBI, in form of promissory note. CD's issued by Banks are available with a maturity period of 7 days to maximum 1 year whereas for FI the time limit is 1 year to 3 year.

d. **Commercial Papers (CP)**[4]: They are issued by corporate or FI in a form of unsecured promissory note and come with a maturity period ranging from 7 day to one year. A company would be eligible to issue CP provided the tangible net worth of the company, as per the latest audited balance sheet, is not less than ₹ 4 crores and has minimum A2 credit rating as per SEBI. Returns are higher than T-bills because of the higher default risk.

e. **Bankers Acceptance**: It is a financial instrument used for International Trade. The BA is a time draft drawn by one party (the drawer) on the bank and accepted by Bank as the Bank's commitment to pay a third party. They come with a maturity period ranging from 30 days to 180 days.

f. **Repurchase Agreement**[5]: Repurchase agreements are like short term loans where buyers and sellers agree to sell and repurchase securities permitted by RBI. Repurchase agreement is apparently done with a promise of purchasing them back particular price and date. They are also termed as 'Repo'. Reverse Repo, is the mirror image of a Repo and involves buying of securities and lending of short term surplus in the first leg and selling the security at a predetermined rate in the second leg. The facility of repurchase agreement between RBI and banks is called LAF (Liquidity Adjustment Facility) and between other participants which include Scheduled Commercial Banks, Co-operative Banks, Primary Dealers, Mutual Funds, Insurance Companies and corporate entities is called Market Repo.

CD, CP and T-Bills are highly traded instruments in money market. T-Bills forms part of eligible securities for Statutory Liquid Ratio (SLR) requirement

[1] https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=9023&Mode=0
[2] https://m.rbi.org.in/Scripts/PublicationsView.aspx?id=16413#3
[3] https://rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?id=8171
[4] https://m.rbi.org.in/Scripts/FAQView.aspx?Id=25
[5] https://www.rbi.org.in/Scripts/PublicationReportDetails.aspx?ID=34

of 18.75% as of today for Banks and FI whereas CD and CP are part of non-eligible securities.

2. CAPITAL MARKET

The capital market refers to the market where borrowers and lenders exchange medium or long-term funds. For raising the funds, the entity may either remain private and raise funds from closed sources (such as friends or relatives of promoters), the financial and strategic investors (such as angel investors, venture capitalists, private equity, etc.) or from banks and other financial institutions, either in form of a debt or equity or a combination of both. Alternately, the entity may reach out to public at large through securities market and proceed with the issue of shares or debt instruments on a recognised stock exchanges. Accordingly, the capital market can also be further categorised into two broad categories. First, the Securities Market i.e. dealing with fresh issue of securities through recognised stock exchanges and further trading thereof and the second being other forms of lending i.e. other than through securities market. Before discussing securities market, firstly, we will discuss the various other forms of lending in a brief.

2.1. Other Forms of Lending and Borrowings:

For raising funds from other than the public at large, the entity may raise funds in form of a debt or arrange funds by way of equity participation of an investor. The various sources of such debt or equity have been discussed below:-

a) **Relatives or Friends:** Easiest source of funds for a promoter is his close relatives and friends. These investors don't ask many tough questions. However, the risk of borrowing is very high as it can lead to risk of social cut-off and humiliation. This sort of funding is also called 'Bootstrapping'.

b) **Banks and Other Financial Institutions:** The most common and traditional way of fulfilling the needs and requirement of funds can be by way of loans obtained from banks or FI, in form of Term Loans, Overdraft Limits, Letter of Guarantee, etc. Funding from these sources is usually secured by way of creation of charge over the assets of the borrower (referred to as the Primary Security). In addition to primary security, banks and FI also require an additional security to further safeguard themselves also known as collateral security.

c) **Angel Investors:** Angel Investors are usually the high net-worth individuals (HNI's) with a successful track record in business who provide with funds to an entrepreneur at a very early stage of the product or concept or idea. They expect a specific rate of return against investment made. The fund size of angel investors is usually between 10 to 50 crores and invests with a typical commitment of 1-5 crores.

d) **Venture Capitalists:** Venture Capitalists (VC) usually enter after angel investors. VC's look for a little bit more stable companies having a strong team and a good track record. They look for an exit opportunity by way of further round of VC funding or through an IPO or acquisition. The fund size of VC's is usually upto 500 crores and invest with a typical commitment of 10-25 crores. To name a few, Helion Ventures, Kalaari Capital, Sequoia Capital, Bessemer Ventures, etc. are some of the VC's.

e) **Private Equity:** Private equity (PE) firms mostly buy out mature companies that are already established. As a result, the PE is in total control of the firm after the buyout. Large institutional investors dominate the private equity world, including pension funds and large private equity firms funded by a group of accredited investors. The fund size of PE is usually above 500 crores and invest with a typical commitment of 50 crores. A few to list are The Blackstone Group, Apollo Global Management, etc.

2.2. Securities Market

In case a person needs funds at large, then part from the above mentioned private sources, he may look for raising funds from public at large through

securities market. In Securities Market for raising funds from public at large, initial step is to issue securities for the first time on a stock exchange by way of an IPO, which automatically results in listing of a security on a recognised stock exchanges for further trading on the recognised stock exchange, also referred to as the Secondary Market. Thus, one can say that the Securities Market has two inter-dependent and inseparable segments, the new issues market (i.e. primary market) and the stock market (i.e. secondary market).In fact, an active secondary market facilitates the growth of primary market as the investors in the primary market are assured of a continuous market for liquidity of their holdings.

2.2.1. Primary market or new issues market

The Primary Market is also referred to as New Issues Market. Here in, the company issues its fresh securities such as shares, debentures or bonds which have not been previously listed on any exchange.

Issue of Shares

In a Primary Market, a company may proceed with the issue of share by way of Initial Public Offering (IPO) and later on by way of Further Public Offering (FPO). The process of IPO is also termed as "going public", as after such a process the company becomes publicly listed on a stock exchange. FPO is also referred as follow-up public offer, where already listed company on stock exchange issues further shares by public offering.

Since public at large is involved who invest their hard-earned money, the primary market is strictly regulated. Listing of Securities on Indian Stock Exchanges is governed by the provisions in the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009, SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, Companies Act, 2013, the Securities Contracts (Regulation) Act, 1956, rules, bye-laws, regulations of concerned stock exchange and circulars/ guidelines issued by the Central Government and SEBI from time to time.

• Stock Exchanges for listing of securities in India

The recognised stock exchanges for issuing securities in India can also be further classified in two categories as per SEBI (Issue of Capital and Disclosure) Regulations 2009 ('ICDR Regulations, 2009'). a) The Main Boards; b) The SME Exchange.

a) The main boards consist of two major exchanges having nationwide terminals as **NSE** and **BSE**.

- National Stock Exchange (NSE)

  The NSE is first demutualised electronic exchange in India and also the world's 12th largest stock exchange. The NIFTY50 is the benchmark index of 50 companies which represent the companies listed on NSE.

- Bombay Stock Exchange (BSE)

  The BSE is oldest stock exchange in Asia is the world's 11th largest stock exchange with more than 5500 companies publicly listed. The S&P BSE SENSEX is the benchmark index for BSE.

b) The SME Exchanges have been recently established in 2012 considering the role of SME (Small and Medium scale Enterprise) in the economy. It consists of two platforms, the BSE offered platform for SME known as **'BSE SME'** and NSE offered

SME platform known as '**Emerge**'. In order to be listed on the SME platform, the SMEs have to proceed with an IPO at any of the aforementioned platforms. The SME after getting itself listed on SME Board also have an option to get itself migrated on main board by passing a special resolution of its shareholders through postal ballot to this effect and if such issuer fulfils the eligibility criteria for listing laid down by the Main Board or the post issue paid up capital is expected to increase beyond ₹ 25 crores.

The key differences as listed below between the main board and SME exchange shall also assist a Company in deciding which board the company may approach for getting its shares listed.

Basis	Main Board IPO	SME Exchange IPO[6]
Post issue paid-up capital	Minimum: ₹ 10 crores	Minimum: ₹ 10 crores Maximum: ₹ 25 crores
Minimum number of allotees	1000	50
Application size	₹ 10,000- ₹ 15,000	Minimum of ₹ 1,00,000
Document Vetting Authority	By SEBI	By stock exchange
Usual Time Frame for Listing	6 months onwards	2-4 months
Norms	Stringent norms as per ICDR Regulations 2009	Relaxed norms
Reporting requirement	Quarterly	Half Yearly
IPO Grading from Credit rating Agency	Non-mandatory	Non-mandatory
IPO Underwriting	Mandatory (however, not required where 50% of the issue offered for subscription to Qualified Institutional Buyers (QIB's)	Mandatory (100% underwritten, out of which 15% compulsorily by Merchant Banker)
Track Record	Three years of track record of profitability	Relaxed norms of Track record

Issue of Debt Securities

Apart from shares, the various types of debt securities, which can also be listed on a stock exchange are:

- Debt Securities of Companies
- Security Receipts by Asset Reconstruction Companies (ARC's)
- Government Securities

The same have been discussed below:-

i. Debt Securities

Apart from shares, debt securities i.e. non-convertible debt securities which create or acknowledge indebtedness and includes debentures, bonds and such other securities of a body corporate or a Trust registered with the SEBI can also be listed on stock exchanges. SEBI has formulated Securities and Exchange Board of India (Issue and Listing of Debt Securities) Regulations, 2008 for issue of debt securities. It must be noted that Convertible Bonds or Debentures are not treated as debt securities.

ii. Security Receipts:

An Asset Reconstruction Company (ARC) functions under SARFAESI Act to buy distressed assets i.e. bad loans of banks/financial institutions at a discount. The securities issued by an ARC as per SEBI (Issue and Listing of Securitised Debt Instruments) Regulations, 2008 ('SDI Regulations') are traded on stock exchange as Security Receipts.

iii. Government Securities

The Government Securities also known as 'G-Sec' or 'Sovereign Bonds' are issued by the RBI on

[6]https://www.sebi.gov.in/legal/regulations/jun-2017/sebi-issue-of-capital-and-disclosure-equirements-regulations-2009-last-amended-on-may-31-2017-_34697.html

behalf of government with original maturity of one year and upto 40 years. G-Sec provide a benchmark for the interest rates prevailing in the country and are also referred to for determination of risk-free rate of return in any economy. The present 10 Year G-Sec Benchmark is '7.26% GS 2029' trading at around 6.60% approx. yield[7]. The various types of securities issued by Government include Fixed Rate Bonds, Floating Rate Bonds (FRB), Capital Indexed Bonds, Inflation Indexed Bonds (IIBs), Bonds with Call/ Put Options, Special Securities under the market borrowing program to entities like Oil Marketing Companies, Fertilizer Companies, the Food Corporation of India, etc. (popularly called oil bonds, fertiliser bonds and food bonds respectively) as compensation to these companies in lieu of cash subsidies, Separate Trading of Registered Interest and Principal of Securities (STRIPS), Sovereign Gold Bond (SGB), etc.[8] Participants of this market comprises of Public Sector Banks, Private Sector Banks, Foreign Banks, Mutual Funds, Primary Dealers, Insurance Companies, etc.

2.2.2. Secondary market

The secondary market comes into the picture immediately after the securities have been listed in the primary market. It is also referred to as stock market where the securities of a company are traded regularly and continuously. The prices of the securities in secondary market are not pre -determined as in case of primary market but are rather determined with the help of demand and supply forces in the market. A retail investor usually trades in secondary market through brokers and sub-brokers.

The portals of the recognised stock exchanges for trading in India are as follows:-

BSE	- BOLT (BSE's On-line trading system)
NSE	- NEAT (National Exchange for Automated Trading)
SME of BSE	- BSE-SME
SME of NSE	- EMERGE

The portals are highly fast and automatic to ensure transparent dealings between the sellers and buyers. SEBI strictly regulates and checks dealings on secondary market as the same is the backbone of India's financial market.

Apart from above well-known stock exchanges, there are portals such as FIMMDA and CCIL which act as support bodies for the market FIMMDA stands for the 'Fixed Income Money Market and Derivatives Association of India'. It is an association of Commercial Banks, FI and Primary Dealers. FIMMDA is a voluntary market body for the Bond, Money and Derivatives Markets. Its objectives include, functioning as the principal interface with the regulators, devise standardised best market practices, to function as an arbitrator for disputes, if any, between member institutions, etc. CCIL on other hand stands for 'Clearing Corporation of India Limited'. It is an institutional infrastructure for clearing and settlement of transactions by banks, FIs, PDs in G-Sec, Foreign Exchange, Money Market and other related products by which counter party credit risk between buyer and seller is eliminated. Both CCIL and FIMMDA play a vital role in reducing counterparty risk, aligning with best global market practices and reducing asset liability mismatches.

The way businesses are done in present global environment keep evolving and so is the requirement of money and instruments dealing in it. Though the Capital Market is very vast and each topic in itself requires an in depth study, however, the above article tries to cover the broad overview of the Capital Market in the country. ■

[7] https://www.nseindia.com/products/content/debt/wdm/gsec_reporting_homepage.htm
[8] https://m.rbi.org.in/Scripts/PublicationsView.aspx?id=16413#3

Earth provides enough to satisfy every man's needs, but not every man's greed. - Mahatma Gandhi