MAR GREGORIOS COLLEGE OF ARTS & SCIENCE

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Affiliated to the University of Madras
Approved by the Government of Tamil Nadu
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DEPARTMENT OF COMMERCE (ACCOUNTING & FINANCE)

SUBJECT NAME: CAPITAL MARKET

SUBJECT CODE: CVG6A

SEMESTER: VI

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Objectives

1. Toexposethestudentstothe worldof capitalmarkets.
2. To enablethestudentstolearn theworkingmechanismofStockexchanges
3. To makethestudentsunderstandtheregulatory framework ofIndian capitalmarkets.

UNITI: Introduction

Financial markets - Definition - Role -Functions-Constituents - Financial Instruments - IndianFinancialMarket-GlobalFinancialMarket-CapitalMarket-Evolutionandgrowth-Constituents - Capital Market Instruments - Types - Preference shares - Equity Shares -Non -voting equity shares - Company fixed deposits - Warrants - Debentures and Bonds- G lobal DebtInstruments.

UNITII:RegulationofIndianCapitalMarket

RegulatoryFramework-CommitteesonRegulatoryFramework-SEBI-Objectives-Management - Powers and functions - Regulatory role - Investor Protection - Insider Trading-Rationale-Insiders -Insiderinformation-Connectedpersons.

UNITIII: StockExchange

History- Meaning - Functions - Stock Exchange Vs Commodity Exchange - Stock ExchangeTraders - Regulation of Stock Exchanges - Steps in Stock Trading - BSE and NSE - World StockExchanges - NewYork,London,Hongkong andTokyoStockExchanges.

UNIT IV: Primary Market Meaning - NIM Vs Secondary Market - Methods of New Issue - Intermediaries in the New issues market - SE BI Guidelines on Primary Market - Listing -Agreement - Benefits - Consequences of Non-listing - Underwriting - Definition - Types -Mechanics - Benefits - Book Building - Concept - Characteristics - Process - IPO including e-IPO-Reversebook-building.

UNITV:OTCEI

Concept - Features - Benefits - OTCE I Vs Other Stock Exchanges - Depository Services- BanksVs Depository - Demat Account - Electronic Settlement of Trade - Role of CDSL and NSDL -Speculation-OnlineStockTrading-DebtMarket-Types-Role-PriceDetermination.

SUGGESTEDREADINGS

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2. FrankJ.Fabozzi,FrancoModigliani,CapitalMarketsInstitutionsandInstrumentsPrenticeHall.2000.NewDelhi.
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E–RESOURCES

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Unit-I

MarketsandFinancialInstruments

TYPESOFMARKETS

Efficient transfer of resources from those having idle resources to others who have apressingneedforthemisachievedthroughfinancialmarkets.Statedformally,financial markets provide channels for allocation of savings to investment. Theseprovide a variety of assets to savers as well as various forms in which the investorscan raise funds and thereby decouple the acts of saving and investment. The saversand investors are constrained not by their individual abilities, but by the economy'sability, to invest and save respectively. The financial markets, thus, contribute toeconomic development to the extent that the latter depends on the rates of savingsandinvestment.

Thefinancialmarketshavetwomajorcomponents:

- Moneymarket
- Capitalmarket.

The **Moneymarket**refers to the market where borrowers and lenders exchangeshort-termfundstosolvetheirliquidityneeds.Moneymarketinstrumentsaregenerally financial claims that have low default risk, maturities under one year andhighmarketability.

The **Capital market** is a market for financial investments that are direct or indirectclaims to capital. It is wider than the Securities Market and embraces all forms oflending and borrowing, whether or not evidenced by the creation of a negotiablefinancial instrument. The Capital Market comprises the complex of institutions andmechanismsthroughwhichintermediatetermfundsandlong-termfundsarepooledand made available to business, government and individuals. The Capital Marketalsoencompassestheprocessbywhichsecuritiesalreadyoutstandingaretransferred.

The**SecuritiesMarket**,however,referstothemarketsforthosefinancialinstruments/claims/obligationsthatarecommonlyandreadilytransferablebysale.

TheSecuritiesMarkethastwointerdependentandinseparablesegments,thenewissues(*primary*)marketandthestock(*secondary*)market.

The *Primary market* provides the channel for sale of new securities. The issuer ofsecurities sells the securities in the primary market to raise funds for investmentand/ortodischargesomeobligation.

The *Secondary market* deals in securities previously issued. The secondary marketenables those who hold securities to adjust their holdings in response to charges intheir assessment of risk and return. They also sell securities for cash to meet theirliquidityneeds.

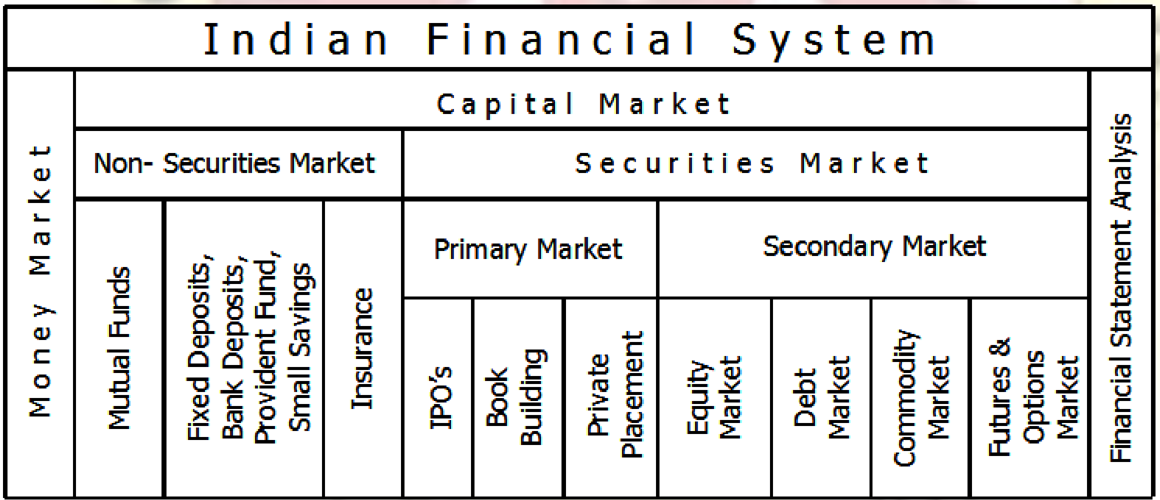
The price signals, which subsume all information about the issuer and his businessincludingassociatedrisk,generatedinthesecondarymarket,helptheprimarym arketinallocationoffunds.

Thissecondarymarkethasfurthertwocomponents.

First,thespotmarketwheresecuritiesaretradedforimmediatedeliveryandpayment.

The other is forward market where the securities are traded for future delivery andpayment. This forward market is further divided into Futures and Options Market(DerivativesMarkets).

In futures Market the securities are traded for conditional future delivery whereas inoption market, two types of options are traded. A **put option** gives right but not anobligationtotheownertosellasecuritytothewriteroftheoptionatapredeterminedprice before a certain date, while a**call option**gives right but not an obligation tothe buyer to purchase a security from the writer of the option at a particular pricebeforeacertaindate.



Letsnowunderstandthesemarketsinbroadersense.

EQUITYMARKET

Beforediscussingtheequitiesmarket,weshould firstunderstand thebasicmeaningofmarkets,theirfunctionsandclassification.

WhatisaMarket?Amarketisalocationwherebuyersandsellers come intocontact to exchange goods or services. Markets can exist in various forms dependingonvariousfactors.

Can Markets Exist in Different Forms? Yes, the markets do exist in different formsdepending on the nature of location and mode of contact. It can have a physicallocation where buyers and sellers come in direct contact with each other or a virtuallocation where the buyers and sellers contact each other employing advance meansof communication. There is another form of market where actual buyers and sellersachievetheirobjectivesthroughintermediaries.

SecuritiesMarkets inIndia: AnOverview:The process of economic reforms andliberalization was set in motion in the mid-eighties and its pace was accelerated in1991 when the economy suffered severely from a precariously low foreign exchangereserve,burgeoningimbalanceontheexternalaccount,decliningindustrialproduction,gallopinginflationandarisingfiscaldeficit.Theeconomicreforms,beingan integrated process, included deregulation of industry, liberalization in foreigninvestment, regime, restructuring and liberalization of trade, exchange rate, and taxpolicies, partial disinvestments of government holding in public sector companiesand financial sector reforms. The reforms in the real sectors such as trade, industryand fiscal policy were initiated first in order to create the necessary macroeconomicstabilityforlaunchingfinancialsectorreforms,whichsoughttoimprovethefunctioning of banking and financial institutions (FIs) and strengthen money andcapitalmarketsincludingsecuritiesmarket.Thesecuritiesmarketreformsspecificallyincluded:

- Repeal of the Capital Issues (Control) Act, 1947 through which Governmentusedtoexpropriateandallocateresourcesfromcapitalmarketforfavoreduses;
- Enactment of the Securities and Exchange Board of India Act, 1992 to providefor the establishment of the Securities and Exchange Board of India (SEBI) toregulateandpromotedevelopmentofsecuritiesmarket;
- Setting up of NSE in 1993, passing of the Depositories Act, 1996 to provide forthemaintenanceandtransferofownershipofsecuritiesinbookentryform;
- Amendments to the Securities Contracts (Regulation) Act, 1956 (SCRA) in 1999toprovidefortheintroductionoffuturesandoption.
- Othermeasuresincludedfreepricingofsecurities,investorprotectionmeasures,useofinformationtechnology,dematerializationofsecurities,improvementin trading practices, evolution of an efficient and transparentregulatory framework, emergence of several innovative financial products andservicesandspecializedFIsetc.

Thesereformsareaimedatcreating efficient andcompetitive securitiesmarketsubjecttoeffectiveregulationbySEBI,whichwouldensureinvestorprotection.

A Profile: The corporate securities market in India dates back to the 18thcenturywhen the securities of the East India Company were traded in Mumbai and Kolkotta.The brokers used to gather under a Banyan tree in Mumbai and under a Neem treein Kolkota for the purpose of trading those securities. However the real beginningcameinthe1850'swiththeintroductionofjointstockcompanieswithlimitedliability.The1860'switnessedfeverishdealingsinsecuritiesandrecklessspeculation. This brought brokers in Bombay together in July 1875 to form the firstformally organized stock exchange in the country viz. The Stock Exchange, Mumbai.Ahmedabad stock exchange in 1894 and 22 others followed this in the 20th century.The process of reforms has led to a pace of growth almost unparalleled in the historyofanycountry.SecuritiesmarketinIndiahasgrownexponentiallyasmeasuredin terms of amount raised from the market, number of stock exchanges and otherintermediaries, the number of listed stocks, market capitalization, trading volumesand turnover on stock exchanges, investor population and price indices. Along withthis,theprofilesoftheinvestors,issuersandintermediarieshavechangedsignificantly. The market has witnessed fundamental institutional changes resultingin drastic reduction in transaction costs and significant improvements in efficiency,transparency and safety, thanks to the National Stock Exchange. Indian market isnowcomparabletomanydevelopedmarketsintermsofanumberofparameters.

StructureandSizeoftheMarkets:Today India has two national exchanges, theBombay Stock Exchange (BSE) and the National Stock Exchange (NSE). Each hasfully electronic trading platforms with around 9400 participating broking outfits.Foreign brokers account for 29 of these. There are some 9600 companies listed onthe respective exchanges with a combined market capitalization near $125.5bn. Anymarket that has experienced this sort of growth has an equally substantial demandfor highly efficient settlement procedures. In India 99.9% of the trades, according totheNationalSecuritiesDepository,aresettledindematerializedforminaT+2rollingsettlementThecapitalmarketisoneenvironment.Inaddition,theNationalSecuritiesClearingCorporationofIndiaLtd(NSCCL)andBankofIndiaShareholdingLtd(BOISL),Clearing CorporationhousesofNSEandBSE,guaranteetradesrespectively.Themainfunctionsof theClearingCorporationaretoworkout(a)whatcounterpartiesoweand(b)whatcounterpartiesareduetoreceiveonthesettlementdate.

Furthermore, each exchange has a Settlement Guarantee Fund to meet with anyunpredictablesituationandanegligibletradefailureof0.003%.TheClearingCorporation of the exchanges assumes the counter-party risk of each member andguaranteessettlementthroughafine-tunedriskmanagementsystemandaninnovativemethodofonlinepositionmonitoring.It alsoensuresthefinancialsettlementoftradesontheappointeddayandtimeirrespectiveof defaultbymemberstodelivertherequiredfundsand/orsecuritieswiththehelpofasettlementguaranteefund.

Style of Operating: Indian stock markets operated in the age-old conventional styleoffact-to-facetradingwithbidsandoffersbeingmadebyopenoutcry.AttheBombayStock Exchange, about 3,000 persons would mill around in the trading ring duringthe trading period of two hours from 12.00 noon to 2.00 p.m. Indian stock marketsbasically quote-driven markets with the jobbers standing at specific locations in thetrading ring called trading posts and announcing continuously the two-way quotesfor the scrips traded at the post. As there is no prohibition on a jobber acting as abroker andvice versa, any memberis freetodojobbing onany day. In actualpractice,however,aclassofjobbershasemergedwhogenerallyconfinetheiractivities to jobbing only. As there are no serious regulations governing the activitiesof jobbers, the jobbing system is beset with a number of problems like wide spreadsbetween bid and offer; particularly in thinly traded securities, lack of depth, totalabsence of jobbers in a large number of securities, etc. In highly volatile scrips,however, the spread is by far the narrowest in the world being just about 0.1 to 0.25percent as compared to about 1.25 per cent in respect of alpha stocks, i.e. the mosthighly liquid stocks, at the International Stock Exchange of London. The spreadswiden as liquidity decreases, being as much as 25 to 30 per cent or even more whilethe average touch of gamma stocks, i.e. the least liquid stocks at the InternationalStockExchange,London,isjustabout6to7percent.Thisisbasicallybecause ofthe high velocity of transactions in the active scrips. In fact, shares in the specifiedgroup account for over 75 percent of trading in the Indian stock markets while over25percentofthesecuritiesdonotgettradedatallinanyyear.Yet,itissignificant to note that out of about 6,000 securities listed on the Bombay Stock Exchange,about1,200securitiesgettradedonanygiventradingday.

The question of automating trading has always been under the active considerationof the Bombay Stock Exchange for quite sometime. It has decided to have trading inall the non-specified stocks numbering about 4,100 totally on the computer on aquote-driven basis with the jobbers, both registered and roving, continuously keyingintheirbidsandoffersintothecomputerwiththemarketordersgettingautomatically executed at the touch and the limit orders getting executed at exactlytheratespecified.

In March 1995, the BSE started the computerized trading system, called BOLT - BSEon-line trading system. Initially only 818 scripts were covered under BOLT. In July1995, all scripts (more than 5,000) were brought under the computerized tradingsystem. The advantages realized are: (a) improved trading volume; (b) reduced spreadbetweenthebuy-sellorders;c)bettertradinginoddlotshares,rightsissuesetc.

Highlightsofthe Highly Attractive Indian Equity Market: Two major reasonswhy Indian securities are now increasingly regarded as attractive to internationalinvestorsaretherelativelyhighreturnscomparedwithmoredevelopedglobalmarketsaswellasthelowcorrelationwithworldmarkets.

DEBTMARKET

The National Stock Exchange started its trading operations in June 1994 by enablingtheWholesaleDebtMarket(WDM)segmentoftheExchange.Thissegmentprovidesa trading platform for a wide range of fixed income securities that includes centralgovernmentsecurities,treasurybills(T-bills),statedevelopmentloans(SDLs),bondsissuedbypublicsectorundertakings(PSUs), floatingratebonds(FRBs),zerocouponbonds (ZCBs), index bonds, commercial papers (CPs), certificates of deposit (CDs),corporate debentures, SLR and non-SLR bonds issued by financial institutions (FIs),bondsissuedbyforeigninstitutionsandunitsofmutualfunds(MFs).

To further encourage wider participation of all classes of investors, including theretailinvestors,theRetailDebtMarketsegment(RDM)waslaunchedonJanuary16,2003. This segment provides for a nation wide, anonymous, order driven, screenbased tradingsystem ingovernmentsecurities.Inthefirst phase, all outstandingand newly issued central government securities were traded in the retail debt marketsegment. Other securities like state government securities, T-bills etc. will be addedin subsequent phases. The settlement cycle is same as in the case of equity marketi.e.,T+2rollingsettlementcycle.

DERIVATIVESMARKET

The emergence of the market for derivative products, most notably forwards, futuresand options, can be traced back to the willingness of risk-averse economic agents toguard themselves against uncertainties arising out of fluctuations in asset prices. Bytheirverynature,thefinancialmarketsaremarkedbyaveryhighdegreeofvolatility.Through the use of derivative products, it is possible to partially or fully transferprice risks by locking–in asset prices. As instruments of risk management, thesegenerallydonotinfluencethefluctuationsintheunderlyingassetprices.

However, by locking-in asset prices, derivative products minimize the impact offluctuations in asset prices on the profitability and cash flow situation of risk-averseinvestors.

DerivativesDefined: Derivative is a product whose value is derived from the valueof one or more basic variables, called bases (underlying asset, index, or referencerate), in a contractual manner. The underlying asset can be equity, forex, commodityor any other asset. For example, wheat farmers may wish to sell their harvest at afuture date to eliminate the risk of a change in prices by that date. Such a transactionisanexampleofaderivative.Thepriceofthisderivativeisdrivenbythespotpriceofwheatwhichisthe“underlying”.

IntheIndiancontexttheSecuritiesContracts(Regulation)Act,1956(SC(R)A)defines “derivative”toinclude–

- A security derived from adebt instrument, share, loan whether secured orunsecured, risk instrument or contract for differences or any other form ofsecurity.
- Acontract,whichderivesitsvaluefromtheprices,orindexofprices,ofunderlyingsecurities.

Derivatives are securities under the SC(R)A and hence the trading of derivatives isgovernedbytheregulatoryframeworkundertheSC(R)A.

Products, Participants and Functions:Derivative contracts have several variants.The most common variants are forwards, futures, options and swaps. The followingthree broad categories of participants - hedgers, speculators, and arbitrageurs tradein the derivatives market. Hedgers face risk associated with the price of an asset.They use futures or options markets toreduce or eliminate this risk. Speculatorswishtobetonfuturemovementsinthe priceofanasset.Futures and optionscontractscangivethemanextraleverage;thatis,theycanincreaseboththepotential gains and potential losses in a speculative venture. Arbitrageurs are inbusiness to take advantage of a discrepancy between prices in two different markets.If, for example, they see the futures price of an asset getting out of line with the cashprice,theywilltakeoffsettingpositionsinthetwomarketstolockinaprofit.

The derivatives market performs a number of economic functions. First, prices in anorganized derivatives market reflect the perception of market participants about thefuture and lead the prices of underlying to the perceived future level. The prices ofderivativesconvergewiththepricesoftheunderlyingattheexpirationofthederivative contract. Thus derivatives help in discovery of future as well as currentprices. Second, the derivatives market helps to transfer risks from those who havethembutmaynotlikethemtothosewhohaveanappetiteforthem.Third,derivatives, due to their inherent nature, are linked to the underlying cash markets.With the introduction of derivatives, the underlying market witnesses higher tradingvolumesbecauseofparticipationbymoreplayerswhowouldnototherwiseparticipate for lack of an arrangement to transfer risk. Fourth, speculative tradesshift to a more controlled environment of derivatives market. In the absence of anorganizedderivativesmarket,speculatorstradeintheunderlyingcashmarkets.Margining,monitoringandsurveillanceoftheactivitiesofvariousparticipantsbecomeextremely difficultinthesekindofmixedmarkets.Fifth,animportantincidental benefit that flows from derivatives trading is that it acts as a catalyst fornewentrepreneurialactivity.Thederivativeshaveahistoryofattractingmanybright,creative, well-educated people with an entrepreneurial attitude. They often energizeothers to create new businesses, new products and new employment opportunities,thebenefitofwhichareimmense.Finally,derivativesmarketshelpincrease savings and investmentin the long run. Transfer of risk enables marketparticipants toexpandtheirvolumeofactivity.

Types of Derivatives: The most commonly used derivatives contracts are forwards,futures and options, which we shall discuss these in detail in the FMM-II later. Herewetakeabrieflookatvariousderivativescontractsthathavecometobeused.

- *Forwards:*A forward contract is a customized contract between two entities,where settlement takes place on a specific date in the future at today's pre-agreedprice.
- *Futures:*A futures contract is an agreement between two parties to buy or sellan asset at a certain time in the future at a certain price. Futures contracts arespecial types of forward contracts in the sense that the former are standardizedexchange-tradedcontracts.
- *Options:*Options are of two types - calls and puts. Calls give the buyer the rightbut not the obligation to buy a given quantity of the underlying asset, at a givenprice on or before a given future date. Puts give the buyer the right, but not theobligation to sell a given quantity of the underlying asset at a given price on orbeforeagivendate.
- *Warrants:*Optionsgenerallyhavelivesofuptooneyear,themajorityofoptionstradedonoptionsexchangeshaving amaximummaturityofninemonths.Longer-dated options are called warrants and are generally traded over-the-counter.
- *LEAPS:*The acronym LEAPS means Long-Term Equity Anticipation Securities.Theseareoptionshavingamaturityofuptothreeyears.
- *Baskets:*Basket options are options on portfolios of underlying assets. Theunderlying asset is usually a moving average or a basket of assets. Equity indexoptionsareaformofbasketoptions.
- *Swaps:*Swaps are private agreements between two parties to exchange cashflows in the future according to a prearranged formula. They can be regardedasportfoliosofforwardcontracts.Thetwocommonlyusedswapsare:
  *Interestrateswap*s:Theseentailswappingonlytheinterestrelatedcashflowsbetweenthepartiesinthesamecurrencyand
  *Currency swap*s: These entail swapping both principal and interest betweenthe parties, with the cash flows in one direction being in a different currencythanthoseintheoppositedirection.
- *Swaptions:*Swaptionsareoptionstobuyorsellaswapthatwillbecomeoperativeattheexpiryoftheoptions.Thusaswaptionisanoptiononaforwardswap.Ratherthanhavecallsandputs,theswaptionsmarkethasreceiverswaptionsandpayerswaptions.Areceiverswaptionisanoptiontoreceivefixedandpayfloating.Apayerswaptionisanoptiontopayfixedandreceivefloating.

TYPESOFINVESTMENTAVENUES

Before starting with the deep discussion on financial markets, we must know in abroad sense about the types of investment avenues available in these markets. Inother words knowing the alternative financial instruments that are bought and soldin these markets. When a person has moremoney than he requires for currentconsumption, he would be coined as a potential investor. The investor who is havingextra cash could invest it in assets like stock or gold or real estate or could simplydeposititinhisbankaccount.Alloftheseactivitiesinabroadersensemeaninvestment.Now,letsdefineinvestment.

HOWDOYOUDEFINEINVESTMENT?

Wecandefineinvestmentastheprocessof,“sacrificing something now for theprospectofgainingsomethinglater”.So,thedefinitionimpliesthatwehavefourdimensions to an investment– time, today’s sacrifice and prospective gain. *Can wethinkofSomeTransactions,whichwillqualifyas“Investments”asperOurDefinition!*

1. Inordertosettledown,ayoungcouplebuysahouseforRs.3lakhsinBangalore.
2. AwealthyfarmerpaysRs.1lakhforapieceoflandinhisvillage.
3. AcricketfanbetsRs.100ontheoutcomeofatestmatchinEngland.
4. Agovernmentofficerbuys‘units’ ofUnitTrustofIndia worthRs4,000.
5. Acollegeprofessorbuys,inanticipationofgoodreturn,100sharesofRelianceIndustriesLtd.
6. AladyclerkdepositsRs.5,000inaPostOfficeSavingsAccount.
7. Based on the rumor that it would be a hot issue in the market in no distantfuture, our friend John invests all hissavingsin the newly floated share issueof Fraternity Electronics Ltd., a company intending to manufacture audio andvideomagnetictapestostartwith,andcinesoundtapesatalaterstage.

Isthereany commonfeatureto allthese investments? A common feature of allthese transactions is that something is sacrificed now for the prospects of gainingsomethinglater.Forexample,thewealthyfarmerintransaction2sacrificesRs.1lakh now for the prospects of crop income later. The lady clerk in transaction 6sacrifices Rs.5,000 now for the prospect of getting a larger amount later due tointerestearned onthesavingsaccount.Thus,inabroad sense,all theseseventransactionsqualifyasinvestment.

Letsnowunderstandtheclassificationofvariousinvestmentalternatives.

FIXED DEPOSITS

The term “fixed” in fixed deposits denotes the period of maturity or tenor. FixedDeposits, therefore, pre-supposes a certain length of time for which the depositordecides to keep the money with the bank and the rate of interest payable to thedepositor is decided by this tenor. The rate of interest differs from bank to bank andisgenerallyhigherforprivatesectorandforeignbanks.This,however,doesnotmeanthat the depositor loses all his rights over the money for the duration of the tenordecided. The deposits can be withdrawn before the period is over. However, theamount of interest payable to the depositor, in such cases goes down (usually 1% to2% less than the original rate). Moreover, as per RBI regulations there will be nointerest paid for any premature withdrawals for the period 15 days to 29 or 15 to 45daysasthecasemaybe.

Other than banks, there are non-banking financial companies and companies whofloat schemes from time to time for garnering deposits from the public. In the recentpast, however, many such schemes have gone bust and it is very essential to lookoutfordangersignalsbeforeputtingallyoureggsinonebasket.

THINGSTOLOOKOUTFOR….

- Creditrating/reputationofthegroup
- Theratingispossiblythebestwaytojudgethecreditworthinessofacompany.However,formanufacturingcompanydeposits,itisnotmandatorytogeta

rating.Insuchcases,itisbettertocheckthesizeandreputationofthecompanyorthein dustrialgroupitbelongsto.

- Interestrate
- Withinthesamesafetylevel(orrating),ahigherinterestrateisabetteroption.Thedifferen ceinsomecasescanbeashighas1%.
- Diversify
- The portfolio principle applies to company deposits also. It is always better tospreaddepositsoverdifferentcompaniesandindustriessoastoreducerisk.
- Period of deposit: The ideal period for a company deposit is 6 months to oneyear as it offers the liquidity option. Also, it gives an opportunity to review thecompany'sperformance.
- Periodic reviewofthecompany:As yourprincipalandinterestrestsinthehandofthecompany,itisadvisabletoreviewthe company'sperformanceperiodically.

WhereNotToInvest?

- Companiesthatoffersveryhighratesofinterest,say16%orabove,whenothersareoffe ring12-13%.
- Companieswithpoorcashflows.
- Avoid unincorporated companies/ private limited companies, as it is difficult tojudgetheirperformanceinabsenceofinformation.
- Companieswithaccumulatedlossesontheirbalancesheets.
- Companieswithapoor dividend payingrecord.

CompanyFixedDeposits

Fixed deposits in companies that earn a fixed rate of return over a period of time arecalled Company Fixed Deposits. Financial institutions and Non-Banking FinanceCompanies(NBFCs)alsoacceptsuchdeposits.Depositsthusmobilizedaregover nedby the Companies Act under Section 58A. These deposits are unsecured, i.e., if thecompany defaults, the investor cannot sell the company to recover his capital, thusmaking them a risky investment option. NBFCs are small organizations, and havemodest fixed and manpower costs. Therefore, they can pass on the benefits to theinvestorintheformofahigherrateofinterest.NBFCssufferfromacredibilitycrisis.Sob eabsolutelysuretocheckthecreditrating.AAAratingisthesafest.Accordingto latest RBI guidelines, NBFCs and companies cannot offer more than 14 per centinterestonpublicdeposits

INVESTMENT OBJECTIVES

AreCompanyFixedDepositsSuitableforanIncreaseinInvestment?

A Company/NBFC Fixed Deposit provides for faster appreciation in the principalamount than bank fixed deposits and post-office schemes. However, the increase intheinterestrateisessentiallyduetothefactthatitentailsmoreriskascomparedtobanksa ndpost-officeschemes.

AreCompanyFixedDepositsSuitableforIncome?

Yes, Company/NBFC Fixed Deposits are suitable for regular income with the optionto receive monthly, quarterly, half-yearly, and annual interest income. Moreover, theinterestratesofferedarehigherthanbanks.

ToWhatExtentDoesaCompany DepositProtectAgainstInflation?

ACompany/NBFCFixedDepositprovidesyouwithlimitedprotectionagainstinflation,withcomparativelyhigherreturnsthanotherassuredreturnoptions.

CanIBorrow againsta CompanyFixed Deposit?

Whether theloans/creditcanbeprovided againstthefixed depositsofthecompany.

RISK CONSIDERATIONS

HowAssuredCanapersonbeOfGettinghisFullInvestmentBack?

CompanyFixedDepositsareunsecuredinstruments,i.e.,thereare no assetsbackingthem up. Therefore, in case the company/NBFC goes under, chances arethat you may not get your principal sum back. It depends on the strength of thecompany and its ability to pay back your deposit at the time of its maturity. Whileinvesting in an NBFC, always remember to first check out its credit rating. Also,bewareofNBFCsofferingridiculouslyhighratesofinterest.

HowAssuredIstheIncome?

Notatallsecured.SomeNBFCshaveknowntodefaultontheirinterestandprincipalpayments. You must check out the liquidity position and its revenue plan beforeinvestinginanNBFC.

AreTheir anyRisksUniquetoCompany FixedDeposits?

If the Company/NBFC goes under, there is no assurance of your principal amount.Moreover, there is no guarantee of your receiving the regular-interval income fromthe company. Inflation and interest rate movements are one of the major factorsaffecting the decision to invest in a Company/NBFC Fixed Deposit. Also, you mustkeep the safety considerations and the company/NBFC's credit rating and credibilityinmindbeforeinvestinginone.

AreCompany/NBFCDepositsratedfortheircreditQuality?

Yes, Company/NBFC Fixed Deposits are rated by credit rating agencies like CARE,CRISIL and ICRA. A company rated lower by credit rating agency is likely to offer ahigher rate of interest and vice-versa. An AAA rating signifies highest safety, and DorFDmeansthecompanyisindefault.

BANKDEPOSITS

When you deposit a certain sum in a bank with a fixed rate of interest and a specifiedtime period, it is called a bank Fixed Deposit (FD). At maturity, you are entitled toreceive the principal amount as well as the interest earned at the pre-specified rateduring that period. The rate of interest for Bank Fixed Deposits varies between 4 and6 per cent,depending on the maturity period of the FD and the amount invested.Theinterestcanbecalculatedmonthly,quarterly,half-yearly,orannually, andvaries from bank to bank.They are one themost common savings avenue, andaccount for a substantial portion of an average investor's savings. The facilities varyfrombanktobank.Someservicesofferedarewithdrawalthroughchequesonmaturity;breakdepositthroughprematurewithdrawal;andoverdraftfacilityetc.

INVESTMENT OBJECTIVES

HowSuitableareFixedDepositsforanIncreaseinInvestment?

While a Bank FD does provide for an increase in your initial investment, it may be atalowerratethanothercomparablefixed-returninstruments.Sincecapitalappreciation in any investment option depends on the safety of that option, andbanksbeingamongthesafestavenues,theincreaseininvestmentismodest.

AreFixedDepositsSuitableForRegularIncome?

A Bank FD does not provide regular interest income, but a lump-sum amount on itsmaturity. Since the lump-sum amount depends on the rate of interest, currentlybetween4and6percent,BankFDsarenotsuitableforregularincome.

ToWhat ExtentDoesaBankFDProtecttheinvestor against Inflation?

With a fixed return, which is lower than other assured return options, banks cannotguardagainstinflation.Infact,thisisthemainproblemwithBankFDsasanyreturn hastobecalculatedkeepinginflationinmind.

CantheinvestorBorrowAgainstBankFDs?

Yes, in some cases, loans up to 90 per cent of the deposit amount can be taken fromthebankagainstfixeddepositreceipts.

RISK CONSIDERATIONS

HowassuredcantheinvestorbeofgettinghisFullInvestmentBack?

Almost 100 per cent. Bank Deposits are the safest investment option after post-officeschemes since the banks function according to the parameters set by the ReserveBank of India (RBI), which frames regulations keeping in mind the interest of theinvestors.

HowAssuredIshisIncome?

There is no regular income in this option as the payment is made in one lump sumaftertheexpiryofthetenureoftheBankFixedDeposit.

AreThereAnyRisksUniqueToBankFDs?

Not really. Since all the banks operating in the country, irrespective of whether theyare nationalized, private, or foreign, are governed by the RBI's rules and regulations,which give due weight age to the interest of the investor, there is little chance of aninvestmentinabankdepositgoingunder.Infact,tillrecently,allbankdepositswereinsuredundertheDepositInsurance&CreditGuaranteeSchemeofIndia,whichhas now been made optional. Nevertheless, bank deposits are still among the safestmodes of investment. The thing to consider before investing in a FD is the rate ofinterest and the inflation rate. A high inflation rate can simply chip away your realreturns. So, it is critical to take the inflation rate into consideration to arrive at therealrateofinterest.

AreBankFDsratedfortheirCreditQuality?

No, Bank FDs are not commercially rated. Since Bank FDs are extremely secure; theonly thing to check out while investing in one is the interest rate being offered andyourconvenience.

InterestRatesPayableonDeposits

Duration	InterestRates(% p.a.)
7daysto14days(Rs.1crandabove)	3.75
15daysto45days	5.00
46daysto179days	5.50
180daysto lessthan 1year	6.50
1yearto lessthan 3years	7.50
3yearstolessthan5years	7.75
5yearsandupto10years	8.00

Source:StateBankofIndia

PublicProvidentFund(PPF)

APublicProvidentFund(PPF)isalong-termsavingsplanwithpowerfultaxbenefits.Yourmoneygrows@8percentperannum,andthisisguaranteedbytheGovernment of India (GOI). You may consider this option if you are not looking forshort-term liquidity or regular income. Normal maturity period is 15 years from thecloseofthefinancialyearinwhichtheinitialsubscriptionwasmade.MaturityvaluesforyourPPFaccountdependingonwhatyouinvesteachyear

RecurringBankDeposits

UnderaRecurringBankDeposit,youinvestaspecificamountinabankonamonthly basis for a fixed rate of return. The deposit has a fixed tenure, at the end ofwhich you get your principal sum as well as the interest earned during that period.Therateofinterest,calculatedquarterlyorasspecifiedbythebank,variesbetween4 and 6 per cent, depending on the maturity period and the amount invested. ARecurringBankDepositisapowerfultoolforregularsavings.

LIFEINSURANCE

Alifeinsurancepolicyisacontractbetweenanindividual(termedasinsured)andaninsurancecompany(insurer)topaytheinsured,orhisnominatedheirs,aspecified sum of money on the happening of an event. The event could be the expiryoftheinsurancepolicyorthedeathoftheinsuredbeforetheexpiry(dateofmaturity) of the policy as per the terms of the policy. In a simple example, a person takes aninsurance policy and nominates his wife as the beneficiary. On the death of thisperson, his wife gets the amount for which the life insurance policy was purchased.Therearemanyvariantsofalifeinsurancepolicy:

1. ***Whole Life Assurance Plans:*** These are low-cost insurance plans where the sumassuredispayableonthedeathoftheinsured
2. ***Endowment Assurance Plans:*** Under these plans, the sum assured is pay-ableon the maturity of the policy or in case of death of the insured individual beforematurityofthepolicy.
3. ***Term Assurance Plans:*** Under these plans, the sum assured is payable only onthedeathoftheinsuredindividualbeforeexpiryofthepolicy.
4. ***Pension Plans:*** These plans provide for either immediate or deferred pension forlife. The pension payments are made till the death of the annuitant (person whohasapensionplan)unlessthepolicyhasprovisionofguaranteedperiod.

Life Insurance Corporation (LIC) is a government company. Till the year 2000, theLICwasthesoleprovideroflifeinsurancepoliciestotheIndianpublic.However,theInsurance Regulatory & Development Authority (IRDA) has now issued licenses toprivate companies to conduct the business of life insurance. Some of the majorprivateplayersinthesectorare:

- BajajAllianzLifeInsurance Corporation
- BirlaSunLifeInsuranceCo.Ltd.
- HDFCStandardLifeInsuranceCo.Ltd.
- ICICIPrudentialLifeInsuranceCo.Ltd.
- INGVysyaLifeInsuranceCo.Pvt.Ltd.
- MAXNewYorkLifeInsuranceCo.Ltd.
- MetLifeIndiaInsuranceCo.Pvt.Ltd.
- KotakMahindraOldMutualLifeInsuranceCo.Ltd.
- SBILifeInsuranceCo.Ltd.
- TATAAIGLifeInsuranceCo.Ltd.
- AMPSanmarAssuranceCo.Ltd.
- AVIVALifeInsuranceCo.Pvt.Ltd.
- SaharaIndiaLifeInsuranceCo.Ltd.
- ShriramLifeInsuranceCo.Ltd.

POSTOFFICESAVINGS

Post Office Savings is an investment option that pays annual interest rate of 3.5percent;Cumulativelycompoundedyearly,andisavailablethroughpost-officesacrossthecountry.

TAXIMPLICATIONS

InvestmentinPostOfficeSavingsaccountforamaximuminvestmentofRs.100,000,per financial year is totally exempt from tax under section 80C of the Income TaxAct, 1961. The Interest Income is also exempted from tax under section 10 of IncomeTaxAct,1961.

PostOfficeSavings:SavingsAccount	
Whocaninvest?	a) SingleAccount • Anindividual(18years&above) • Aminorwhohasattainedtheageof10years • Aguardianonbehalfofaminor

	• Aguardianofapersonofunsoundmi nd
	b) JointAccount–Twoorthreeadults
Howmuchyoucaninvest?	• SingleAccount–MinimumRs.20andupto Rs.1lac • JointAccount–MinimumRs.20anduptoRs.2lac
Howmuchdoyouearn?	3.5
%When interestiscompounded?	YearlyWhe
ninterestispaid?	YearlyCum
ulative/Non-cumulative?	Cumulative
Whenyoucanwithdraw?	Anytime
What doyou get onredemption?	AmountbalanceintheaccountPr
emature withdrawalfacility?	Notapplicable
Prematurewithdrawalterms?	Anytime
Marketability?	Verygood
Isitsafe?	Very safe
Isitsecured?	Secured
Isitconvenient?	• OpenatanyPostOffices • Chequefacility • Minimumbalancelow
Canyougetaloan?	Notapplicable
Istheincometaxable?	TotallytaxfreeU/s80cofIncomeTaxAct,1961Anyo
thertaxconcessions?	Interest incomeexemptedfromincometaxU/s 10ofIncomeTaxAct,1961Is
nominationfacilityavailable?	Yes

PostOfficeSavings:RecurringDepositAccount

Whocaninvest?	a)ASingleadult b) Twoadultsjointly,theamountdueontheacco untbeingpayable • Tobothjointlyorsurvivor • Toeitherofthemorsurvivor c) Aguardianonbehalfofaminororapersonofuns oundmind d) Aminorwhohasattainedtheageoftenyear sinhisownname
Howmuchyoucaninvest?	Rs.10permonthtoanyamountHo
wmuchdoyouearn?	7.5%
When interestiscompounded?	QuarterlyW
heninterestispaid?	YearlyCumu
lative/Non-cumulative?	Cumulative
Whenyoucanwithdraw?	After5years • Extension ofaccountaftermaturityperiod:Continueacc ount,maybeforafurtherperiodoffiveyearsan dmakemonthlydepositsduringsuchextende dperiod. • Retentionofamountofrepaymentbeyondmat urityperiod:TheDepositormayathisoption,co ntinuetheaccountandretaininittheamountofr epaymentdueforafurtherperiodupto

	maximumoffiveyearswithoutmakinganyfres hdeposits.
What doyou get onredemption?	
	AmountbalanceintheaccountPr
emature withdrawalfacility?	After3years
Prematurewithdrawalterms?	
	Onlyonceupto50%ofthebalanceMar
ketability?	Good
Isitsafe?	Verysafe
Isitsecured?	Secured

Isitconvenient?	OpenatanyPostOffices
Canyougetaloan?	50%ofthedepositsmadeintheaccountmaybeallowedasloanaftertheaccounthasbeenin operationforatleastoneyear
Istheincometaxable?	• Taxable • NoTDS • NoWealthTax
Anyothertaxconcessions?	Rebateonadvancedeposits • Deposits–Six ormorebutnotexceedingelevendepositsmadeinacalendarmonth;Rebate–Rs.10foran account ofRs.100denomination • Deposits–Twelveormoredepositsmadeinacalendarmonth; Rebate– Rs.40 foreverytwelvedepositsofRs.100denomination
Isnominationfacilityavailable?	Yes

SMALLSAVINGS

SmallSavingsSchemesarebasicallyoftwotypes:

- ***PostOfficeSavings:***Savings Deposits; Recurring Deposits; Time Deposits; &MonthlyIncomeAccountand
- ***NationalSavings:***PublicProvidentFund;NationalSavingsCertificates;&KisanVikasPatra

WehavealreadydiscussedthecharacteristicsofPostOfficeSavings&PublicProvident Fund in the earlier sections in this chapter; we further summarize thefeaturesoftheremainingsmallsavingsproducts.

NationalSavings:PublicProvidentFund(PPF)	
Whocaninvest?	a) AnIndividual(above18years) b) HinduUndividedFamily c)AguardianonbehalfofaminorMinimumR
Howmuchyoucaninvest?	s.500anduptoRs.70,000per annum
Howmuchdoyouearn?	8%
Wheninterest iscompounded?	Yearly
Wheninterestispaid?	Onmaturity
Cumulative/Non-cumulative?	Cumulative
Whenyoucanwithdraw?	After15years • Extension ofaccount–Account maybeextendedforanyblockperiodoffiveyears
Whatdoyougetonredemption?	Entirebalanceintheaccount
Prematurewithdrawalfacility?	6thYearto15thYear
Prematurewithdrawal terms?	Onceinayearupto50%ofthebalancein4th precedingorprecedingyearwhicheverislower
Liquidity?	Good
Isitsafe?	Verysafe
Isitsecured?	• Secured • EvencourtscannotattachthePPFbalance
Isitconvenient?	• OpenatanyPostOffices • Orspecifiedbank
Canyougetaloan?	From3rdto6thYear

	• Upto25%oftheamountavailableintheprec eding2ndyear
Istheincometaxable?	Totallytaxfree
Anyothertaxconcessions?	• RebateU/s80cofIncomeTaxAct,1961 • NoWealthTaxI
s nominationfacilityavailable?	Yes

NationalSavings:NationalSavingsCertificates(NSCVIII)

Whocaninvest?	a)AnIndividual(above18years) b) Twoindividuals c) Aguardianonbehalfofaminor
Howmuchyoucaninvest?	MinimumRs.100anduptoanyamount,in denomination ofRs.100,Rs.500,Rs.1000andRs.10,000
Howmuchdoyouearn?	8%
When interestiscompounded?	
	HalfYearly
Wheninterestispaid?	On
maturityCumulative/Non-cumulative?	
	Cumulative
Whenyoucanwithdraw?	After6year
What doyou get onredemption?	
	AmountoutstandingwithinterestP
remature withdrawalfacility?	Inexceptionalcases
Prematurewithdrawalterms?	
	OnthedeathoftheholderoranyoftheholdersLiqui
dity?	Good
Isitsafe?	Verysafe
Isitsecured?	Secured
Isit convenient?	OpenatanyPostOffices
Canyougetaloan?	Canbepledgedasasecurityforloans
Istheincometaxable?	• Taxable • NoTDS
Anyothertaxconcessions?	• Annualaccruedinterestisalsoeligiblefor rebateU/s80cofIncomeTaxAct,1961 • NoWealthTaxI
s nominationfacilityavailable?	Yes

NationalSavings:KisanVikasPatra(KVP)

Whocaninvest?	a)AnIndividual(above18years) b) Twoorthreeindividualsin joint names c) Aguardianonbehalfofaminor
Howmuchyoucaninvest?	MinimumRs.100anduptoanyamount,in denominationofRs.100,Rs.500,Rs.1000,Rs.10,000a ndRs.50,000
Howmuchdoyouearn?	8.25%
approximatelyWhen interestiscompounded?Yearly	
Wheninterestispaid?	
	OnmaturityCum
ulative/Non-cumulative?	
	CumulativeWhen
youcanwithdraw?	8years7months
What doyou get onredemption?	
	DoubletheamountinvestedP
remature withdrawalfacility?	Availableafter2.5years
Prematurewithdrawalterms?	Earlywithdrawalatfixedratesanytimeincase ofdeath ofholderoranyoftheholders
Liquidity?	Poor
Isitsafe?	Verysafe
Isitsecured?	Secured
Isit convenient?	OpenatanyPostOffices

Canyougetaloan?	Canbepledgedasasecurityforloans
Istheincometaxable?	• Taxable • NoTDS

Anyothertaxconcessions?	• NoWealthTax
Isnominationfacilityavailable?	Yes

GOLD

Ofallthechoiceofinvestmentsavailable,can this yellow metal take pride of theplace as a financial investment alternative option? Opinion on the subject of gold isdivided,onseveral issues – are the yields from an investment in gold positive? Areitsusesproductive?Isthestrainontheeconomyevident?Shouldgoldbeallowedtobebroug htintoIndiafreelyforpurposesofinvestmentorotherwise?

Well, yields or no yields, there is hardly an Indian household that can ignore goldandkeepitsentiresavingsinfinancialassetsalone.Everyinvestmenthasanintrinsic appeal to its holder and to suggest that hundreds of tones of gold is boughtevery year without regard to its economic value is to suggest that Indians don't actrationally.Thefactis,theydoandprobablydoitbetterthanothers.

Indian's faith in GOD and GOLD dates back to the Vedic times; they worshippedboth. According to the World Gold Council Report, India stands today as the world'slargest single market for gold consumption. In developing countries, people haveoftentrustedgoldasabetterinvestmentthanbondsandstocks.Goldis animportantandpopularinvestmentformanyreasons:

- In many countries gold remains an integral part of social and religious customs,besidesbeingthebasicformofsaving. Shakespeare called it 'the saint–seducinggold'.
- Superstition about the healing powers of gold persists. Ayurvedic medicine inIndiarecommendsgoldpowderandpillsformanyailments.
- Goldisindestructible.It does not tarnish andisalso not corrodedby acid – exceptbyamixtureofnitricandhydrochloricacids.
- Goldhasaestheticappeal.Itsbeautyrecommendsitforornamentmakingaboveallot hermetals.
- Goldissomalleablethatoneounceofthemetalcanbebeatenintoasheetcoveringnear lyahundredsquarefeet.
- Goldissoductilethatoneounceofitcanbedrawnintofiftymilesofthingoldwire.
- Goldisanexcellentconductorofelectricity;amicroscopiccircuitofliquidgold 'printed'onaceramicstripsavesmilesofwiringinacomputer.
- GoldissohighlyvaluedthatasinglesmugglercancarrygoldworthRs.50lacundernea thhisshirt.
- Goldissodensethatallthetonesofgold,whichhasbeenestimated;tobeminedthroug hhistorycouldbetransportedbyonesinglemodernsupertanker.
- Finally,goldisscam-free.Sofar,therehavebeennoMundra–typeorMehta–typescamsingold.

Apparently, gold is the only product, which has an investment as well as ornamentalvalue. Going beyond the narrow logic of yield and maturity values, thus, the lure ofthisyellowmetalcontinues.

EQUITYSHARE

Equity, also called shares or scrips, is the basic building blocks of a company. Acompany's ownership is determined on the basis of its shareholding. Shares are, byfar, the most glamorous financial instruments for investment for the simple reasonthat, over the long term, they offer the highest returns. Predictably, they're also theriskiestinvestmentoption.

TheBSESensexisthemostpopularindexthattracksthemovementsofsharesof30 blue-chip companies on a weighted average basis. The rise and fall in the valueoftheSensex,measuredinpoints,broadlyindicatestheprice-movementofthevalueof shares. Of late, technology has played a major role in enhancing the efficiency,safety,andtransparencyofthemarkets.Theintroductionofonlinetradinghas madeitpossibleforaninvestortotradeinequitiesattheclickofamouse.

DEBENTURES/BONDS

A Bond is a loan given by the buyer to the issuer of the instrument. Companies,financial institutions, or even the government can issue bonds. Over and above thescheduled interest payments as and when applicable, the holder of a bond is entitledtoreceivetheparvalueoftheinstrumentatthespecifiedmaturitydate.

Bondscanbebroadlyclassifiedinto:

- Tax-SavingBonds
- RegularIncomeBonds

Tax-SavingBondsoffertaxexemptionup toaspecified amountofinvestment,examplesare:

a. ICICIInfrastructureBondsunderSection88oftheIncomeTaxAct,1961
b. RECBondsunderSection54ECoftheIncomeTaxAct,1961
c. RBITaxReliefBonds

Regular-IncomeBonds,asthenamesuggests,aremeanttoprovideastablesourceofincomeatregular,pre-determinedintervals,examplesare:

a. DoubleYourMoneyBond
b. Step-UpInterestBond
c. RetirementBond
d. En-cashBond
e. EducationBonds
f. MoneyMultiplierBonds/DeepDiscountBond

Tax-SavingBonds

Some bonds have a special provision that allows the investor to save on tax. Theseare termed as Tax-Saving Bonds, and are widely used by individual investors as atax-savingtool.Examplesofsuchbondsare:

a. InfrastructureBondsunderSection88oftheIncomeTaxAct,1961
b. CapitalGainsBondsunderSection54ECoftheIncomeTaxAct,1961
c. RBISavingsBonds(erstwhile,RBIReliefBonds)d.
e. ***WhatareTaxSavingInfrastructureBonds?*** Infrastructure bonds areavailablethroughissuesofICICIBankandIDBI,broughtoutinthenameofICICISafetyBondsand IDBIFlexibonds.Theseprovidetax-savingbenefitsunderSection88oftheIncomeTaxAct,1961,uptoaninvestmentof Rs.1,

00,000,subjecttothebondsbeingheld foraminimum periodofthreeyearsfromthedateofallotment.

Unit–II Primary Market

PRIMARYMARKETS

Companiesraisefundstofinancetheirprojectsthroughvariousmethods.Thepromoters can bring their own money of borrow from the financial institutions ormobilize capital by issuing securities. The funds mayberaised through issue of freshsharesatparorpremium,preferencesshares,debenturesorglobaldepositoryreceipts.Themainobjectivesofacapitalissuearegivenbelow:

- To promoteanewcompany
- Toexpandanexistingcompany
- Todiversifytheproduction
- Tomeettheregular workingcapitalrequirements
- Tocapitalizethereserves

Stocks available for the first time are offered through primary market. The issuermay be a new company or an existing company. These issues may be of new type orthesecurityusedinthepast.Intheprimarymarkettheissuercanbeconsideredasa manufacturer. The issuing houses, investment bankers and brokers act as thechannel of distribution for the new issues. They take the responsibility of selling thestockstothepublic.

THEFUNCTION

The main service functions of the primary market are origination, under writing anddistribution. Origination deals with the origin of the new issue. Theproposal isanalyzed in terms of the nature of the security, the size of the issue, timing of theissue and floatation method of the issue. Underwriting contract makes the sharepredictableandremovestheelementofuncertaintyinthesubscription(underwritingis given in the latter part of this chapter). Distribution refers to the sale of securitiestotheinvestors.Thisiscarriedoutwiththehelpoftheleadmanagersandbrokerstotheissue.

THERISEANDFALLOFPRIMARYMARKETS

Only a few years back, any investor worth his salt thought that investing in primaryissueswastheeasiestandsimplestwaytomakemoney.Hescoffedatother“inferior”options like mutual funds and bank depositsbecause they did not double or triplehismoneyina fewmonthstime!Believeitornot,primarymarketsdidthatprecisely – they posted near indecent returns like 300 to 400% just in two months time. Whenthecommoninvestorbenchmarkedallotherinvestmentoptionsagainstthesephenomenal returns, obviously they stood no chance. Returns apart, investing inprimary issues appeared so simple and “risk free”! All that was required of investorstopartakeinthemannawastosimplyputaslargeanapplicationas possiblebecausetheproportionateallotmentruleworkedtothefavorofbiginvestors(small investorsweresupposedtohavegonetomutualfunds)andprayforalargeallotment.Oncet heyreceivedsomesharesonthelargesubscription,theyjustoffloaded their holdings at the listed prices, which were at a hefty premium to theissue price not because of any good fundamentals of the issuing company but simplybecausedemandwasfargreaterthanthesupplyandwaitedforthenextIPOtomakea notherkilling.

As profit booking became so simple, money flowed from all directions, some legal andsomenotsolegal–themarkets boomed and promoters, brokers and investors allmade merry. "Entrepreneurs" of all sorts mushroomed to float companies with fancyprojectsandlaunchedIPOswithtallpromises to give high earnings and dividends.But no one bothered to check the prospectuses or the credentials of these promotersbecause there was enough moneyto be made by every one or so they thought, untilthemarketscrashedliketheproverbialninepins.

What drove the primary markets to these dizzy heights only to collapse later? Thosewere theearlydaysofliberalizationandtheforeigninstitutionalinvestorsandmutua l funds had no clue as to the levels of transparency or corporate governanceabsent in the Indian companies. They believed in the picture specially painted forthem by the wily promoters, liked it and invested heavily believing in what was rightin the West would be right in the East as well. They were rudely shaken when thepromised projects failed to take off because of rampant diversion of money, plainincompetenceandseverechangeintheeconomicclimate.

Thencame,theicewinterofstockmarket gloom, which lasted for probably thelongest period in the near history. As investors lost money and faith in the primarymarket,theypunishedalltheissuers–IPOafter IPO failed to get the desiredresponse from the markets – it almost became impossible for any company to raisemoneyfromthestockmarkets.Genuinecompanies,whichlinedupon-goingprojectsfor funds to be raised from the market were driven to desperation and borrowed atusurious rates that broke the back of their balance sheets. The high cost of borrowingmade debt servicing difficult and defaults occurred even from corporate organizationsknownfortheirhighcreditworthiness.

TheSouthAsiancrisisfurthermadelife very difficult for Indian entrepreneurs astheirexportsfailedtotakeoffandmoneygotlockedupinhugeinventories.Thiswasthe perfect recipe for disaster and doomsayers were busy writing the epitaph on theIndian economic revival. As the economy teetered on the verge of collapse, the outlookhaschangedslowlybutsurely– softwaresectorcametotherescueofthemarkets,afewrobustcompaniesliftedthemarketfrom their lowest depths to the presentpeaksofunprecedentedhighs.

AndtheBullRunbeganalloveragain.Marketsareinfrenzywithinstitutionalbuyingandast heindexzoomedto14500levels,theprimarymarketissueswerebackwithabang.Doyouse eanyredherringshere?

Many analysts said investors were climbing up the same learning curve all overagain.Someofthe'companies'thatcameoutwithIPOshardlyhadtherightcredentials or performance track record to justify the public offer. But the investorsstarved so long for 'good' issues were merrily lapping up all of them. Happily so far,they all made money as the scripts listed above their issue prices posted handsomereturnsinvery shortterm.Butdon'tthehappeningsappearsodisturbinglyfamiliar?

If you were a discerning investor, you would know speculation and serious investingareverydifferent.Asourdiscursionheredealswiththesecond,we makeanattempt to list the factors that an investors should consider as achecklist to guide yourprimarymarketinvestments.

FACTORSTOBECONSIDEREDBYTHEINVESTORS

The number of stocks, which has remained inactive, increased steadily over the pastfew years, irrespective of the overall market levels. Price rigging, indifferent usage offunds, vanishing companies, lack of transparency, the notion that equity is a cheapsourceoffundandthepermittedfreepricingoftheissuersareleadingtotheprevailingprimarymarketconditions.

In this context, the investor has to be alert and careful in his investment. He has toanalyzeseveralfactors.Theyaregivenbelow:

Factorsto beconsidered:

Promoter's Credibility	• Promoter's past performance with reference to the companiespromotedbythemearlier. • Theintegrityofthepromotersshouldbefoundoutwithenquiriesandfromfinancialmagazinesandnewspapers. • Theirknowledge andexperiencein therelatedfield.
Efficiencyofthe Management	• The managing director's backgroundandexperience inthe field. • The composition of the Board of Directors is to be studiedto find out whether it is broad based and professionals areincluded.
ProjectDetails	• Thecredibilityoftheappraisinginstitutionoragency. • Thestakeoftheappraisingagencyintheforthcomingissue.
Product	• Reliabilityofthedemandandsupplyprojectionsoftheproduct. • Competitionfacedinthemarketandthemarketingstrategy. • Iftheproductisexportoriented,thetie-upwiththeforeigncollaboratororagencyforthepurchaseofproducts.
FinancialData	• Accountingpolicy. • Revaluationoftheassets,ifany. • Analysisofthedatarelatedtocapital,reserves,turnover,profit, dividendrecordandprofitabilityratio.
Litigation	• Pending litigations and their effect on the profitability of thecompany. Default in the payment of dues to the banks andfinancialinstitutions.
RiskFactors	• Acarefulstudyofthegeneralandspecificriskfactorsshouldbecarriedout.

Auditor'sReport	•	Athroughreadingoftheauditor'sreportisneededespecially with reference to significant notes to accounts,qualifying remarks and changes in the accounting policy.In the case of letter of offer the investors have to look forthe recently audited working result at the end of letter ofoffer.
StatutoryClearance	•	Investor should find out whether all the required statutoryclearance has been obtained, if not, what is the currentstatus.Theclearancesusedtohaveabearingonthecompletionoftheproject.
InvestorService	•	Promptness in replying to the enquiries of allocation ofshares, refund of money, annual reports, dividends andsharetransfershouldbeassessedwiththehelpofpast record.

INVESTORSPROTECTIONINTHEPRIMARYMARKET

Toensurehealthygrowthofprimarymarket,theinvestingpublicshouldbeprotected.Theterminvestor'sprotectionhasawidermeaningintheprimarymarket.Theprincipalingredientsofinvestorprotectionare:

- Provisionofalltherelevantinformation,
- Provisionofaccurateinformationand
- Transparentallotmentprocedureswithoutanybias.

To provide the above-mentioned factors several steps have been taken. They areprojectappraisal,underwriting,clearanceoftheissuedocumentbythestockexchange andSEBI'sscrutinyoftheissuedocument.

Project Appraisal: This is the first step in the entire process of the project. Technicalandeconomicfeasibilityoftheprojectisevaluated.Iftheprojectitselfisnottechnically feasible and economically viable, whatever may be the other steps takentoprotecttheinvestorsaredefeated.Appraisalshowswhethertheprojectismeaningful and can befinanced. The investors'protection starts rightfrom theprotection of the principal amount of investment. Based on the appraisal, the projectcostisfinalized.Thecostshouldbeneitherunderstandnoroverstated.Theprofitability of the project should be estimated and given. To ensure fair projectappraisal,SEBIhasmadeitmandatoryfortheprojectappraisalbodytoparticipateacertainamountintheforthcomingissue.

Underwriting:Oncetheissueisfinalizedtheunderwritingprocedurestarts.Reputedinstitutionsandagencies,providingcredibilitytotheissuenormallyunderwrite the issue. If the lead managers participate more than 5 percent of theminimum stipulated amount offered to the public, it would increase the confidenceofthepublicregardingthepricingandsaleabilityoftheissue.

Disclosures in the Prospectus: SEBI has issued stringent norms for the disclosureof information in the prospectus. It is the duty of the lead manager to verify theaccuracy of the data provided in the prospectus. The pending litigation should begiven clearly. The promoters' credibility in fulfilling the promises of the previousissues(ifany)shouldbestated.Aclearversionoftheriskfactorsshouldbegiven.

Any adverse development that affects the normal functioning and the profit of thecompanyshouldbehighlightedintheriskfactor.

Clearancebythe Stock Exchange: The issue document has to be cleared by thestock exchange on which the proposed listing is offered. The stock exchanges verifythe factors related with the smooth trading of the shares. Any bottleneck in this areawill be eliminated since the transferability is the basic right of the shareholders.Tradingofthe shareshelpstheinvestortoliquidatehisshareatanytime.Ifthe issueswere not traded in the secondary market at a good price, they would dampen thespirit of the investor. According to a study conducted by Mr. PrithviHaldea, betweenApril 1992 and March 1996 out of 3,872 issues, 2,987 were traded below the offerprice. As on January 14, 1997 nearly 205 shares were not traded at all and another118companiesjustprovedtobeflybynightoperators.

Signing by Board of Directors: The Board of Directors should sign the prospectus.A copy is also filed with the office to the Registrar of the Companies. This along withtheothermaterialdocumentsreferredtointheprospectusareavailableforinspection by the members of the public. The minimum amount to be subscribed bythe promoters and maintained for a minimum number of years also safeguards theinterestoftheinvestors.

SEBI's Role: (a) SEBI scrutinizes the various offer documents from the viewpoint ofinvestors'protectionandfulldisclosure.Ithasthepowertodeletetheunsubstantiated claims and ask for additional information wherever needed. Thismakestheleadmanagertopreparetheofferdocumentwithduecareanddiligence; (b) Whenthedisclosureoftheinformationiscomplete,widepublicityhastobegivenin the newspapers; (c) In the allotment procedure to make sure of transparency,SEBI'snomineeisappointedapartfromthestockexchangenomineeintheal lotmentcommittee. Inclusion of valid applications and rejection of invalid applications arechecked. The representative of the SEBI see to it that un-due preference is not giventocertaingroupofinvestors.

RedressalofInvestorsGrievances:TheDepartmentofCompanyAffairshasintroducedco mputerizedsystemofprocessingthecomplaintstohandleiteffectively.The companies are requested to give feed back regarding the action taken on eachcomplaint within a stipulated time period. If the companies do not respond and areslow in the process of settlement of complaints, penal action can be taken againstthe companies under the provisions of the Companies Act. If the performance of theRegistrar to the issue is not satisfactory in settling the complaints, SEBI can takeappropriate action against such Registrar. Several Investors Associations are alsofunctioningtohelptheinvestorscomplaintsredressedpromptly.

PRIMARYMARKETTRENDS-OVERNINETIES

The liberalization policy adopted by the government in the early nineties resulted ina boom in the secondary market. The boom was not restricted to the secondarymarket alone, the primary market that till then was working under the Controller ofCapital Issue also enjoyed the boom with the repealing of the Controller of CapitalIssueAct.Withthedawnofaneraoffreepricingmoreandmorecompaniesaccessed theprimarymarket.

There was a fall in the amount raised through primary market from March 1995 withmuch-publicized M.S. shoe episode. This episode put a break on the new issuesactivity.ThecollapseoftheCRBcapitalmarketwasanotherfatalblowontheprimary market.Theprimarymarketwasdullandinsipidin1997-98.Thenumberofprimaryissues,whichwere813in1996-97drastically,felldownto62issuesin

1997-98. It is interesting to note that out of every 100 public issues 39 was oversubscribed in 1995-96 but in 1996-97 it was 8. At the same time 7 out of every 100companies in 1996-97 had to return application money to investors for failing toraise minimum stipulated amount in capital issue. The reasons for this sordid stateofaffairsaregivenbelow.

AggressivePricing:Thisisthemajor cause for thesorrystateof affairsintheprimary market. The near complete freedom given to the issuers and the merchantbankers to fix the premium following the repeal of Capital Issue Act resulted in highpremium, sharp erosion of post listing prices and very little scope for appreciation.Thismadetheinvestorstoshyawayfromthemarket.

Poor Liquidity: The poor quality of the primary issues has contributed to a growinginactive list in the stock market. A glance at the profile of the in active scrips as onJune1997,providesaninterestinginsightofthe3617scripsthatwereon theinactive list (based on trading in the first half of 1997). In those shares, 2,900 werelisted prior to 1996 and 1,200 were companies listed prior to 1994. There is no wayout for the investors and their fears have resulted in poor response to the primarymarket.

LowReturns: Non-implementation of projects, delays, changes in the scope andscale of projects to justify the cost and non-attainment of projected earnings haveresulted in the fall in listing price. Though large sums were raised in 1992-96 period,capital formation with concomitant earnings has been nowhere near that reflected intheofferdocuments.Poorreturnshavedrainedtheinvestors' confidence.

Low Volume: The scrips that are traded in the market, the number of transactionsand the amount traded are so low that an investor wanting to sell the scrip wouldhavedifficultyindoingso.ManyscripsinthecurrentB1groupshowthistrend.

EconomicSlowDown:ThegrowthoftheGDPhasfallenfrom7percentin1995-96 to mere 6 per cent in 1996-97. Recession faced-by the economy had a directimpactonthesecondary andtertiary sector. Ithad anindirecteffectupon theprimarymarket.

One should not jump to the conclusion that there are no takers in primary market.Eventodaytherearetakersforgoodqualityissues.Severalnewissuesbythebanks - both private and public sectors have proved to be quite a success on the stockmarketintherecentpast.StockslikeHDFCBank,GlobalTrustBank,SatyamComputers,Infosysetc.areperformingwellonthestockmarket.

The year 1999 saw renewed entrees in the primary market. The initial public offerfromcompaniesofITsectorwasreceivedwell.Thefundsmobilizedthroughthedebtand equity route aggregated to Rs.54,352cr, a rise of around 24 per cent comparedRs.44,115croresin1998.

MEASURESTAKENTOREVIVETHEMARKET

- A listed company having immediate three years of dividend paying track recordonlycanaccessthemarket.
- Ifamanufacturingcompanydidnothavesuchatrackrecord,itcouldaccessthepublicissuemarketprovidedthefinancialinstitutionorascheduledcommercialbankappraiseditsprojectandsuchappraisingentitiesalsoparticipatedintheprojectfund.

- The companies were required to complete the allotment of securities within 30daysoftheclosureoftheissue.
- Itwouldbenecessaryforacorporatebodymakingapublicissuetohaveatleast five public shareholders who has been made a net capital offer to the tuneofRs.1lakhforever.
- SEBIdoesnotvetofferdocumentsofcompanieshavingtrackrecordof3yearsdividen dpayment.
- Removalofmandatoryrequirementof90percentsubscriptionclauseincasesofoffer forsale.
- ReducingtheminimumapplicationsizeforsubscribingtoapublicissuefromRs.500 0toRs.2000.
- In case of no-underwritten public issues, promoters could bring in their ownmoney or procure subscription from elsewhere within 60 days of the closure oftheissuesubjecttosuchdisclosuresintheofferdocuments.
- SEBIliftedtheprovisionofthelockinperiodforpromoters'contributionincase oflistedcompanieswith3yearstrackrecordofdividend.
- SEBI has made it mandatory to disclose un-audited results of companies foreveryquarter.Timelyinformationwouldnowbeavailabletothepublic.
- SEBI has directed different stock exchange to segregate the cash flow statementof all companies that came out with IPO since 1992-93 and have asked theexchangetohaveacheckoverthesecompanies.
- SEBI abolished the fixed par value concept and, instead companies can fix theparvalueoftheshares.HCLTechnologiesIPOhasaparvalueofRs.4pershare,offe redatRs.580pershare.

PRIMARYMARKETFOREQUITY-TODAY

Primary market for equity, which consists of both the 'initial public offering' (IPO)market and the 'seasoned equity offering' (SEO) markets, experienced considerableactivity in 2004 and 2005 (see Table below). In 2005, Rs.30,325crore of resourceswere raised on this market, of which Rs.9,918 crore were made up by 55 companieswhich were listed for the first time (IPOs). The number of IPOs per year has risensteadily from 2002 onwards. A level of 55 IPOs in the year translates to roughly 4IPOs every month. The mean IPO size, which was elevated in 2004, returned toRs.180crore,whichissimilartothevalueprevalentin2003.

The primary issuance of debt securities, as per SEBI, fell to a low of around Rs. 66crore in 2005, which is one facet of the far-reaching difficulties of the debt market.Unlike equity securities, companies redeem debt securities issued at previous datesevery year. Hence, a year with a low issuance of fresh debt securities is a year inwhichthestockofoutstandingdebtsecuritiesdrops.

Table:PrimaryMarket *(Rs.crores)*

	CalendarYear			
	2002	**2003**	**2004**	**2005**
Debt	4,549	5,284	2,383	66
Equity	2,420	2,891	33,475	30,325
Ofwhich, IPOs	1,981	1,708	12,402	9,918
NumberofIPOs	6	12	26	55
MeanIPOsize	330	142	477	180
Total	6,970	8,175	35,859	30,391
Number	28	43	65	109

Source:SEBI

In addition to resource mobilization by the issuance of debt and equity securities,one of the most important mechanisms of financing that has been used by Indianfirmsisretainedearnings,whicharealsoapartofequityfinancing.

Primarily, issues can be classified as a Public, Rights or Preferential issues (alsoknown as private placements). While publicand rights issues involve a detailedprocedure,privateplacementsorpreferentialissuesarerelativelysimpler.Theclassificationofissuesisillustratedfurther.

INITIALPUBLICOFFER(IPO)

PartiesInvolvedintheIPO

In the sixties and seventies, the company and its personnel managed IPO. But, atpresentinitialpublicofferinginvolvesanumberofagencies.Therulesandregulations,thechangingscenarioofthecapitalmarketnecessitatedthecompanyto seek for the support of many agencies to make the public issue a success. As astudent of financial market management, one should know the number of agenciesinvolvedandtheirrespectiveroleinthepublicissue.Thepromotersalsoshouldhavea clear idea about the agencies to coordinate their activities effectively in the publicissue.Themanagertotheissue,registrarstotheissue,underwriters,bankers,advertisingagencies,financialinstitutionsandgovernment/statutoryagencies.

MANAGERSTOTHEISSUE

Lead managers are appointed by the company to manage the initial public offeringcampaign.Theirmaindutiesare:

- Draftingofprospectus
- Preparingthebudgetofexpensesrelatedtotheissue
- Suggestingtheappropriatetimingsofthepublicissue
- Assistinginmarketingthepublicissuesuccessfully
- Advisingthecompanyintheappointmentofregistrarstotheissue,underwriters,brokers,bankerstotheissue,advertisingagentsetc.
- Directingthevariousagenciesinvolvedinthepublicissue.

Many agencies are performing the role of lead managers to the issue. The merchantbankingdivisionofthefinancialinstitutions,subsidiaryofcommercialbanks,foreign banks, private sector banks and private agencies are available to act as leadmangers. Such as SBI Capital Markets Ltd., Bank of Baroda, Canara Bank, DSPFinancialConsultantLtd.ICICISecurities&FinanceCompanyLtd.,etc.Thecompany negotiates with prospective mangers to its issue and settles its selectionandtermsofappointment.Usuallycompaniesappointleadmanagerswithasuccessful background. There may be more than one manager to the issue. Sometimes the banks or financial institutions impose a condition while sanctioning termloan or underwriting assistance to be appointed as one of the lead managers to theissue. The fee payable to the lead managers is negotiable between the company andtheleadmanager.Thefeeagreeduponisrevealedinthe memorandumoftheunderstandingfiledalongwiththeofferdocument.

REGISTRARTOTHEISSUE

After the appointment of the lead managers to the issue, in consultation with them,the Registrar to the issue is appointed. Quotations containing the details of thevarious functions they would be performing and charges for them are called forselection. Among them the most suitable one is selected. It is always ensured thatthe registrar to the issue has the necessary infrastructure like Computer, Internetandtelephone.

TheRegistrarsnormallyreceivetheshareapplicationfromvariouscollectioncenters.They recommend the basis of allotment in consultation with the Regional StockExchange for approval. They arrange for the dispatching of the share certificates.They hand over the details of the share allocation and other related registers to thecompany. Usually registrars to the issue retain the issuer records at least for a periodof six months from the last date of dispatch of letters of allotment to enable theinvestorstoapproachtheregistrarsforredressaloftheircomplaints.

UNDERWRITERS

Underwriting is a contract by means of which a person gives an assurance to theissuer to the effect that the former would subscribe to the securities offered in theevent of non-subscription by the person to whom they were offered. The person whoassures is called an underwriter. The underwriters do not buy and sell securities.Theystandasback-upsupportersandunderwritingisdoneforacommission.Underwritingprovidesaninsuranceagainstthepossibilityofinadequatesubscription.Underwritersaredividedintotwocategories:

- FinancialInstitutionsandBanks
- Brokersandapprovedinvestmentcompanies.

Some of the underwriters are financial institutions, commercial banks, merchantbankers, members of the stock exchange, Export and Import Bank of India etc. Theunderwriters are exposed to the risk of non-subscription and for such risk exposuretheyarepaidanunderwritingcommission.

Beforeappointinganunderwriter,thefinancialstrengthoftheprospectiveunderwriter is considered because he has to undertake and agree to subscribe thenon-subscribedportionofthepublicissue.Theotheraspectsconsideredare:

- Experienceintheprimarymarket
- Pastunderwritingperformanceanddefault
- Outstandingunderwritingcommitment
- The networkofinvestorclientele ofthe underwriter and
- Hisoverallreputation.

The company after the closure of subscription list communicates in writing to theunderwriterthetotalnumberofshares/debenturesundersubscribed,thenumberof shares/debentures required to be taken up by the underwriter. The underwriterwould take up the agreed portion. If the underwriter fails to pay, the company is freeto allot the shares to others or take up proceeding against the underwriter to claimdamagesforanylosssufferedbythecompanyforhisdenial.

BANKERSTOTHEISSUE

Bankerstotheissuehavetheresponsibilityofcollectingtheapplicationmoneyalongwith the application form. The bankers to the issue generally charge commissionbesidesthebrokerage,ifany.Dependinguponthesizeofthe publicissuemorethan one banker to the issue is appointed. When the size of the issue is large, 3 to 4 banksare appointed as bankers to the issue. The number of collection centers is specifiedby the central government. The bankers to the issue should have branches in thespecifiedcollectioncenters.Inbigormetropolitancitiesmorethanonebranchofthevariousbankerstothe issue aredesignated as collecting branches. Branches arealsodesignatedinthedifferenttownsofthestatewheretheprojectisbeingsetup.If the collection centers for application money are located nearby people are likely toinvestthemoneyinthecompanyshares.

ADVERTISINGAGENTS

Advertising plays a key role in promoting the public issue. Hence, the past trackrecord of the advertisingagencyisstudied carefully. Tentativeprogram of eachadvertising agency along with the estimated cost are called for. After comparing theeffectivenessandcostofeachprogramwiththeother,asuitableadvertisingagencyif selected inconsultation with theleadmanagerstotheissue. Theadvertisingagencies take the responsibility of giving publicity to the issue on the suitable media.Themediamaybenewspapers/magazines/hoardings/pressreleaseoracombinationofall.

THEFINANCIALINSTITUTIONS

Financial institutions generally underwrite the issue and lend term loans to thecompanies.Hence,normallytheygothrough thedraft ofprospectus,studytheproposed program for public issue and approve them. IDBI, IFCI & ICICI, LIC, GICand UTI are the some of the financial institutions that underwrite and give financialassistance. The lead manager sends copy of the draft prospectus to the financialinstitutionsandincludestheircomments,ifanyintherevideddraft.

GOVERNMENTANDSTATUTORYAGENCIES

Thevariousregulatorybodiesrelatedwiththepublicissueare:

- SecuritiesExchangeBoardofIndia
- Registrar ofcompanies
- ReserveBankofIndia(iftheprojectinvolvesforeigninvestment)
- StockExchangewheretheissueisgoingtobelisted
- Industriallicensingauthorities
- Pollutioncontrolauthorities(clearancefortheprojecthastobestatedintheprospectus)

COLLECTIONCENTERS

Generally there should be at least 30 mandatory collection centers inclusive of theplaces where stock exchanges are located. If the issue is not exceeding Rs.10 Cr(excludingpremiumifany)themandatorycollectioncentersarethefourmetropolitancentersviz.Mumbai,Delhi,KolkattaandChennaiandatallsuchcenterswherestockexchangesarelocatedintheregioninwhichtheregisteredofficeof the company is situated. The regional divisions of the various stock exchanges andtheplacesoftheirlocationsaregiveninthefollowingtable.

Region	*Exchange*	*City*
NorthernRegion	LudhianaStockExchangeD elhiStockExchangeJaipur StockExchange UPStockExchange	Ludhiana DelhiJaip urKanpur

Southern Region	HyderabadStockExchangeBangaloreStockExchangeMangaloreStockExchangeMadrasStockExchangeCoimbatoreStockExchangeCochinStockExchange	HyderabadBangaloreMangaloreChennaiCoimbatoreCochin
Eastern Region	CalcuttaStockExchangeGawahatiStockExchangeMagadhStockExchangeBhubaneswarStock Exchange	KolkattaGawahatiPatnaBhubaneswar
WesternRegion	Bombay StockExchangeNationalStockExchangeOTCELStockExchangeMPStockExchangePuneStockExchange VadodaraStockExchangeAhmedabadStockExchangeSauashtraKutchStockExchange	MumbaiMumbaiMumbaiIndorePuneVadodaraAhmedabadRajkot

Inadditiontothecollectionbranch,authorizedcollectionagentsmayalsobeappointed. The names and addresses of such agent should be given in the offerdocuments. The collection agents are permitted to collect such application money intheformofcheques,draft, andstock-investsandnotintheformofcash. Theapplication money so collected should be deposited in the special share applicationaccount with the designated scheduled bank either on the same day or latest by thenextworkingday.

Theapplicationcollectedbythebankerstotheissueatdifferentcentersareforwardedtothe Registrarafterrealizationofthecheques,withinaperiodof2weeksfrom the date of closure of the public issue. The applications accompanied by stock-invests are sent directly to the Registrars to the issue along with the schedules withinone week from the date of closure of the issue. The investors, who reside in placesother than mandatory and authorized centers, can send their application with stock-investStotheRegistrartotheissuedirectlybyregisteredpostwithacknowledgementduecard.

PlacementoftheIPO

Initial public offers are floated through Prospectus; Bought out deals/offer for sale;PrivatePlacement;RightIssueandBookBuilding.

OFFERTHROUGHPROSPECTUS

AccordingtoCompanies(Amendment)Act1985,applicationformsforsharesofacompanyshouldbeaccompanied by aMemorandum (abridgedprospectus). Insimple terms a prospectus document gives details regarding the company and invitesoffers for subscription or purchase of any shares or debenturesfrom the public. Thedraft prospectus has to be sent to the Regional Stock Exchange where the shares ofthecompanyaretobelistedandalsotoallotherstockexchangeswherethesharesare proposed to be listed. The stock exchange scrutinizes the draft prospectus. Afterscrutiny if there is any clarification needed, the stock exchange writes to the companyandalsosuggestsmodificationifany.Theprospectusshouldcontaindetailsregarding the statutory provisions for the issue, program of public issue– opening,closing and earliest closing date of the issue, issue to be listed at, highlights and riskfactors,capitalstructure,boardof directions, registered office of the company,brokerstotheissue,briefdescriptionoftheissue,costof the project, projectedearningsandothersuchdetails.The board, lending financial institutions and thestockexchangesinwhichtheyaretobelistedshouldapprovetheprospectus.

Prospectusisdistributedamongthestockexchanges,brokersandunderwriters,collecting branchesofthebankersandtotheleadmanagers.

SalientFeaturesoftheProspectus:

GeneralInfo rmation	• Nameandaddressoftheregisteredofficeofthecompany. • The name(s) of the stock exchange(s) where applicationshave been made for permission to deal in and for officialquotationsofshares/debentures. • Opening,closingandearliestclosingdatesoftheissue. • Nameandaddressofleadmanagers. • NameandaddressofTrusteesunderDebentureTrustDeed(in caseofdebentureissue). • Rating for debenture/preference shares, if any, obtainedfromCRISILoranyotherrecognizedratingagency.
CapitalStructur eoftheCompany	• Issued,subscribedandpaid-upcapital. • Sizeofthepresentissuegivingseparatelyreservationforprefer entialallotmenttopromotersandothers. • Paid-upcapital–(a)Afterthepresentissueand(b)Afterconversionofdebentures(ifap plicable). • Detailsregarding thepromoter'scontribution.
TermsoftheP resentIssue	• Authority for the issue, terms of payment, procedure andtime schedule for allotment, issue of certificate and rightsoftheinstrumentholders. • How to apply– availability of forms, prospectus and modeofpayment. • Specialtaxbenefitstothecompanyandshareholdersunderthe IncomeTaxAct,ifany.
ParticularsoftheI ssue	• Objectoftheissue • Projectcost • Meansoffinancing(includingpromoter'scontribution).
Company,Manag ement andProject	• History, main objects and present business of thecompany. • Subsidiary(ies)ofthecompany,ifany. • Promotersandtheirbackground. • Names, addresses and occupation of managing directorsandotherdirectorsincludingnomineedirectorsand whole-timedirectors. • Location ofthe project. • Plantandmachinery,technologicalprocessetc. • Collaboration,anyperformanceguaranteeorassistanceinma rketingbythecollaborators. • Infrastructurefacilitiesforrawmaterialsandutilitieslikewate r,electricityetc. • Scheduleofimplementationoftheprojectandprogresssofar, giving details of land acquisition, civil works,

installationofplantandmachinery,trailproduction,consumerproductionetc.

- The Product– (a) Nature of the products– Consumer orIndustrialandtheendusers; (b) Approach to marketingand proposed marketing set-up; (c) Export possibilities andexportobligations,ifany.
- Future prospects – expected capacity utilization during thefirstthreeyearsfromthedateofcommencementofproduction and the expected year when the company wouldbeabletoearncashprofitandnetprofit.
- Stockmarketdataforshares,debenturesofthecompany(high–lowpriceforeachofthelastyearsinconsideration).
- Particulars regarding the other listed companies under thesame management, which have made any capital issuesduringthelastthreeyears.

Outstanding Litigations

- Details of the outstanding litigations pertaining to matterslikely to affect the operations and finances of the companyincluding disputed tax liabilities of any nature, any otherdefaultandcriminalprosecutionlaunchedagainstthecompany.

RiskFactors

- Management perception of risk factors like sensitivity toforeignexchangeratefluctuations,difficultyintheavailability of raw materials or in marketing of products,cost,timeover-runetc.

Justification oftheissuepremium

Thejustificationforpriceisgiven,takingintoaccountthefollowingparameters:

- Performanceofthecompany–reflectedbyearningspershareandbookvalueofsharesforthepast fiveyears.
- FutureprojectionsintermsofEPSandbookvalueofsharesinthenextthreeyears.
- Stockmarketdata.
- Netassetvalueasperthelatestauditedbalancesheet.

If the projections are not based on the past data, appraisalmadebyabankerorfinancialinstitutionshouldbespecificallystated.

FinancialInformation

- Financial performance of the company for last five yearsshouldbegivenfromtheauditedannualaccountsintabularform.
- Balancesheetdate–equitycapital,reserves(revaluationreserve, the year of revaluation and its monetary effect onassets)andborrowings.
- Profitandlossdata–sales,grossprofit,netprofit,anddividendpaid,ifany.
- Any change in the accounting policy during the last threeyearsanditseffectontheprofitandreservesofthe company.

Statutoryandoth erinformation	• Minimumsubscription. • Details of the fee payable to Advisers, Registrar, Managers,Trusteesofthedebentureholdersandunderwriters. • Detailsregardingthepreviousissues,ifany.

BOUGHTOUTDEALS(OFFERFORSALE)

Here, the promoter places his shares with an investment banker (bought out dealeror sponsor) who offers it to the public at a later date. In other works in a bought outdeal, an existing company off-loads a part of the promoters' capital to a wholesalerinstead of making a public issue. The wholesaler is invariably a merchant banker orsome times just a company with surplus cash. In addition to the main sponsor, therecould be individuals and other smaller companies participating in the syndicate. Thesponsors hold on to these shares for a period and at an appropriate date they offerthe same to the public. The hold on period may be as low as 70 days or more than ayear.

In a bought out deal, proving is the essential element to be decided. The bought outdealer decides the price after analyzing the viability, the gestation period, promoters'backgroundandfutureprojections.Aboughoutdealershedsthesharesatapremiumtothepublic.Therearemanyadvantagesfortheissuingcompany:

- ***Firstly,*** a medium or small sized company, which is already facing workingcapital shortage, cannot afford to have long lead-time before the funds could bemobilized from the public. Bought out deal helps the promoters to realize thefundswithoutanylossoftime.
- ***Secondly,*** the cost of raising funds is reduced in bought out deals. For issuingshare to the public the company incurs heavy expenses, which may invariablybeashighas10percentofthecostoftheproject,ifnotmore.
- ***Thirdly,*** bought out deal helps the entrepreneurs who are not familiar with thecapital market but have sound professional knowledge to raise funds. Sponsorsofthedealaremostlyconcernedwiththepromoters'backgroundandgovernment policies than about the past track record or financial projections.Thishelpsthenewentrepreneurtoraiseadequatecapitalfromthemarket.
- ***Fourthly,*** for a company with no track record of projects, public issues at apremiummayposeproblems,asSEBIguidelinescomeintheway.Thestipulationscanbeavoidedbyaboughtoutdeal.Companiessellthesharesata premium to the sponsors and they can off-load the shares to the public at ahigherpremium.
- ***Fifthly,*** to the investors bought out deals possess low risk since the sponsorshave already held the shares for a certain period and the projects might havebeen completed or may be in the verge of completion, the investors need notwaitforreturns

Themajordisadvantageoftheboughtoutdealsisthatthesponsorsareabletocreateapositiveimageaboutthesharesandsellthemataheftypremium.Singleinvestment banker gives scope for manipulation of the results. Insider trading andpriceriggingcouldbecarriedout,whichcanbeneitherdetectednorpenalized.

PRIVATEPLACEMENT

In this method the issue is placed with a small number of financial institutions,corporatebodiesandhighnetworthindividuals.Thefinancialintermediariespurchase the shares and sell them to investors at a later date at a suitable price. Thestockisplacedwithissuehouseclientwiththemediumofplacingletterandother documents which taken together contribute a prospectus, giving the informationregardingtheissue.Thespecialfeatureoftheprivateplacementisthattheissu esare negotiated between the issuing company and the purchasing intermediaries.Listed public limited company as well as closely held private limited company canaccessthepublicthroughtheprivateplacementmethod.Mostlyintheprivateplaceme nt securities are sold to financial institutions like Unit Trust of India, mutualfunds,insurancecompanies,andmerchantbankingsubsidiariesofcommercialba nksandsoon.

Through private placement equity shares, preference shares, cumulative convertiblepreferenceshares,debenturesandbondsaresold.InIndiaprivateplacement marketis witnessing the introduction of several innovative debt market instruments such asstep-down/step-up debentures, liquid debentures, bonds etc. Private placement hasseveralinherentadvantages:

- ***CostEffective:*** Private placement is a cost-effective method of raising funds. Inapublicissueunderwriting,brokerage,printing,mailingandpromotionaccountf or8to10percentoftheissuecost.Inthecaseoftheprivateplacementseveralstatutory andnon-statutoryexpensesareavoided.

- ***Time Effective:*** In the public issue the time required for completing the legalformalities and other formalities takes usually six months or more. But in theprivate placement the requirements to be fulfilled are less and hence, the timerequiredtoplacetheissueisless,mostly2to3months.

- ***StructureEffectiveness:***Itcanbestructuredtomeettheneedsoftheentrepreneurs.It isflexibletosuittheentrepreneursandthefinancialintermediaries. To make the issue more attractive the corporate can providediscounts to the intermediaries who are buying it. This is not possible with thepublic issue with stringent rules and regulations. In the case of debentures theinterest ceiling cannot be breached in a public issue. Here the terms of the issuecanbenegotiatedwithpurchasinginstitutionseasilysincetheyarefewinnumbe r.

- ***AccessEffective:***Throughprivateplacementapubliclimitedcompanylistedorunlist edcanmobilizecapital.Like-wiseissueofallsizecanbeaccommodatedthrough the private placement either small or big where as in the public issuemarket,thesizeoftheissuecannotfallbelowacertainminimumsize.

RIGHTSISSUE

AccordingtoSec81oftheCompaniesAct1956,ifapubliccompanywantstoincreaseitssubs cribedcapitalbyallotmentoffurthersharesaftertwoyearsfromthe date of its formation or one year from the date of its first allotment, which ever isearlier should offer share at first to the existing share holders in proportion to theshares held by them at the time of offer. The shareholders have no legal binding toaccept the offer and they have the right to renounce the offer in favor of any person.Shares of this type are called right shares. Generally right shares are offered at anadvantageousratecomparedwiththemarketrate.

According to Section 81, the company has to satisfy certain conditions to issue rightshares.

- Right shares must be offered to the equity shareholders in the proportion to thecapitalpaidonthoseshares.

- Anoticeshouldbeissuedtospecifythenumberofsharesissued.
- Thetimegiventoaccepttherightoffershouldnotbelessthan15days.
- The notice also should state the right of the shareholders to renounce the offerinfavorofothers.
- After the expiry of the time given in the notice, the Board of Directors has theright to dispose the unsubscribe shares in such a manner, as they think mostbeneficialtothecompany.

BOOKBUILDING

Book building is a mechanism through which the initial public offerings (IPOS) takeplace in the U.S. and in India it is gaining importance with every issue. Most of therecent new issue offered in the market has been through Book Building process.Similar mechanisms are used in the primary market offerings of GDRs also. In thisprocess the price determination is based on orders placed and investors have anopportunityto place ordersat different prices aspracticedininternationalofferings.

The recommendations given by Malegam Committee paved way for the introductionofthebookbuildingprocessinthecapitalmarketinOct1995.Bookbuildingin volvesfirm allotmentofthe instrumentto a syndicatecreated by the lead managers whosell the issue at an acceptable price to the public. Originally the potion of bookbuildingprocesswasavailabletocompaniesissuingmorethanRs.100cr.Therestricti ononthеminimumsizewasremovedandSEBIgaveimpressiontoadoptthebook building method to issue of any size. In the prospectus, the company has tospecify the placement portion under book building process. The securities availableto the public are separately known as net offer to the public. Nirma by offering amaximum of 100 lakh equity shares through this process was set to be the firstcompanytoadoptthemechanism.

Among the lead managers or the syndicate members of the issue or the merchantbankers as member. The issuer company as a book runner nominates this memberand his name is mentioned in the draft prospectus. The book runner has to circulatethe copy of the draft prospectus to be filed with SEBI among the institutional buyerswho are eligible for firm allotment. The draft prospectus should indicate the pricebandwithinwhichthesecuritiesarebeingofferedforsubscription.

The offers are sent to the book runners. He maintains a record of names and numberofsecuritiesofferedandthepriceofferedbytheinstitutionalbuyerwithintheplace ment portion and the price for which the order is received to the book runners.The book runner and the issuer company finalize the price. The issue price for theplacementportionandoffertothepublicshouldbethesame.Underwritingagreementi senteredintoafterthefixationoftheprice.

One day earlier to the opening of the issue to the public, the book runner collects theapplicationformsalongwiththeapplicationmoneyfromtheinstitutionalbuyersandth e underwriters. The book runner and other intermediaries involved in the bookbuildingprocess should maintain records ofthe book building process. The SEBIhastherighttoinspecttherecords.

BOOKBUILDINGTHROUGHONLINEIPO

Book building as discussed earlier is a process of offering securities in which bids atvarious prices from investors through syndicate members are collected. Based onbids,demandforthesecurityisassessedanditspricediscovered.Incaseofnormal public issue, investor knows the price in advance and the demand is known at theclose of the issue. In case of public issue through book building, demand can beknownattheendofeverydaybutpriceisknownattthecloseofissue.

An issuer company proposing to issue capital through book building has two optionsviz., 75% book building route and 100% book building route. In case of 100% bookbuilding route is adopted, not more than 60% of net offer to public can be allocatedto QIBs (Qualified Institutional Buyers), not less than 15% of the net offer to thepublic can be allocated to non-institutional investors applying for more than 1000shares and not less than 25% of the net offer to public can be allocated to retailinvestors applying for up to 1000 shares. In case 75% of net public offer is madethrough book building, not more than 60% of the net offer can be allocated to QIBsand not less than 15% of the net offer can be allocated to non-institutional investors.The balance 25% of the net offer to public, offered at a price determined throughbookbuilding,areavailabletoretailindividualinvestorswhohaveeithernotparticipated in book building or have not received any allocation in the book builtportion. Allotment to retail individual or non-institutional investors is made on thebasisofproportionalallotmentsystem.Incaseofundersubscriptioninanycategory,the un-subscribed portions are allocated to the bidder in other categories. The bookbuiltportion, 100%or 75%,asthecasemaybe,ofthenetoffer topublic,arecompulsorilyunderwrittenbythesyndicatemembersorbookrunners.

Otherrequirements forbookbuildinginclude:

- Bidsremainopenforatleast5days.
- Onlyelectronicbiddingispermitted.
- Bidsaresubmittedthroughsyndicatemembers.
- Bidscanberevised.
- Biddingdemandisdisplayedattheendofeveryday.
- Allotmentsaremadenotlaterthan15daysfromtheclosureoftheissueetc.

The100%bookbuildinghasmadetheprimaryissuanceprocesscomparativelyfasterandcosteffectiveandtradingcancommencefromT+16.

The SEBI guidelines for book building provides that the company should be allowedtodisclosethefloorprice,justpriortotheopeningdate,insteadofintheRedherring prospectus,whichmaybedonebyanymeanslikeapublicadvertisementinnewspaper etc. Flexibility should be provided to the issuer company by permittingthem to indicate a 20% price band. Issuer may be given the flexibility to revise theprice band during the bidding period and the issuers should be allowed to have aclosedbookbuildingi.e.thebookwillnotbemadepublic.Themandatoryrequirement of 90% subscription should not be considered with strictness, but theprospectusshoulddisclosetheamountofminimumsubscriptionrequiredandsources formeetingtheshortfall.ThePrimaryMarketAdvisoryCommitteerecommended the practice of ‘green-shoe option’ available in markets abroad whichis an ‘over allotment’ option granted by the issuer to the underwriter in a publicoffering. This helps the syndicate member to over allocate the shares to the extent ofoption available and to consequently purchase additional shares from the issuer attheoriginalofferingpriceinordertocovertheover-allotments.

ON-LINE INITIALPUBLICOFFERS(IPO)

A company proposing to issue capital to public through on-line system of the stockexchange has to comply with Section 55 to 68A of the Companies Act, 1956 and SEBIGuideline, 2000. The company is required to enter into an agreement with the stockexchange(s),whichhavetherequisitesystemforon-lineofferofsecurities.The agreementshouldcoverrights,duties,responsibilitiesandobligationsofthecompany and the stock exchanges inter-se, with provision for a dispute resolutionmechanismbetweenthecompanyandthestockexchange.Theissuercompanya ppointsaRegistrartotheIssuehavingelectronicconnectivitywiththestockexchanges. The issuer company can apply for listing of its securities at any exchangethroughwhichitoffersitssecuritiestopublicthroughon-linesystem,apartfromtherequirementoflistingontheregionalstockexchange.Thestocke xchangeappoints brokers for the purpose of accepting applications and placing orders withthe company. The lead manager would co-ordinate all the activities amongst variousintermediariesconnectedinthesystem.

In addition to the above, the SEBI guidelines also provide details of the contents ofthe offer document and advertisement, other requirements for issues of securities,like those under Rule 19(2)(b) of SC(R) Rules, 1957. The guidelines also lay downdetailed norms for issue of debt instruments, Issue of capital by designated financialinstitutionsandpreferential/bonusissues.

BOOKBUILDINGTHROUGHON-LINEIPOSYSTEM

Book building is basically a process used in IPO for efficient price discovery, whereinduring the period for which the IPO is open, bids are collected from investors atvariousprices,whichareaboveorequaltothefloorprice.Theofferpriceisdetermined after the bid closing date. In it's strive to continuously improve IndianSecurities Market; NSE offers its infrastructure for conducting online IPOs throughbook building. It helps to discover price as well as demand for a security to be issuedthroughaprocessofbiddingbyinvestors.Theadvantagesofthisnewsystemare:

- Theinvestorpartswithmoneyonlyafterallotment,
- Iteliminatesrefundsexceptincaseofdirectapplicationsand,
- Itreducesthetimetakenforissueprocess.

The securities get listed within 15 days from the closure of the issue. Though theguidelines for book building were issued in 1995, it is being used for IPOs from 1999.Till June 2003, 19 issuers have used this route for making IPO issues. During 2002-03,twoissuersusedtheon-lineIPOsystemofNSEtoissue71.66lakhshares.

ELIGIBILITYTOISSUESECURITIES

The issues of capital to public by Indian companies are governed by the Disclosureand Investor Protection (DIP) Guidelines of SEBI, which were issued in June 1992.SEBI has been issuing clarifications to these guidelines from time to time aiming atstreamlining the public issue process. In order to provide a comprehensive coverageof all DIP guidelines, SEBI issued a compendium series in January 2000, known asSEBI (DIP) Guidelines, 2000. The guidelines provide norms relating to eligibility forcompaniesissuingsecurities,pricingofissues,listingrequirements,disclosurenorms, lock-in period for promoter's contribution, contents of offer documents, pre-and post-issue obligations, etc. The guideline applies to all public issues, offers forsaleandrightsissuesbylistedandunlistedcompanies.

Eligibility Norms: Any company issuing securities through the offer document hastosatisfythefollowingconditions:

- AcompanymakingapublicissueofsecuritieshastofileadraftprospectuswithSEBI,t hroughaneligiblemerchantbanker,atleast21dayspriortothe filing of prospectus with the Registrar of Companies (RoCs). The filing of offerdocument is mandatory for a listed company issuing security through a rightsissuewheretheaggregatevalueofsecurities,includingpremium,if any,exceeds Rs.50 lakh. A company cannot make a public issue unless it has madeanapplicationforlistingofthosesecuritieswithstockexchanges(s).Thecompany must also have entered into an agreement with the depository fordematerialization of its securities and also the company should have given anoptiontosubscribers/shareholders/investorstoreceivethesecuritycertificates or securities in dematerialized form with the depository. A companycannot make an issue if the company has been prohibited from accessing thecapitalmarketunderanyorderordiscretionpassedbySEBI.

- Anunlistedcompanycanmakepublicissueofequitysharesoranyothersecurity convertible into equity shares, on fixed price basis or on book buildingbasis,provided:
  (i) It has a pre-issue net worth of not less than Rs.1 crore in 3 out of thepreceding5yearsandhasminimumnetworthinimmediatelyprecedingtwoyears,
  (ii) It has a track record of distributable profits in terms of section 205 of theCompanies Act, 1956, for at least 3 out of immediately preceding 5 years,and
  (iii) The issue size (offer through offer document + firm allotment + promoterscontribution through the offer document) does not exceed five times its pre-issuenetworth.
  (iv) Alistedcompanyiseligibletomakeapublicissue,onfixedpricebasisoron book building basis, if the issue size does not exceed five times its pre-issuenetworth.

  If the company, listed or unlisted, does not meet the above criteria, then theissue will have to be compulsorily made through book building route. In such acase, 60% of the issue size will have to be allotted to the 'Qualified InstitutionalBuyers'(QIBs)failingwhichthefullsubscriptionmoneyshallberefunded.

- Infrastructure companies are exempt from the requirement of eligibility normsiftheirprojecthasbeenappraisedbyapublicfinancialinstitutionorinfrastructure development finance corporation or infrastructure leasing andfinancing services and not less than 5% of the project cost is financed by any oftheinstitutions,jointlyorseverally,bywayofloanand/orsubscriptiontoequityor a combination of both. Banks and rights issues of listed companies are alsoexemptfromtheeligibilitynorms.

- For public and rights issues of debt instruments irrespective of their maturitiesor conversion period, it is mandatory to obtain credit rating from a registeredcreditratingagencyandtodisclosethesameintheofferdocument.Ifthecreditratingisobtainedfrommorethanonecreditratingagency,allthecreditratings,includingtherejectedones,needtobedisclosed.Forapublicandrightsissueof debt securities with issue size greater than or equal to Rs.100 crore, creditrating from two rating agencies is mandatory. In case of issue of debentureswith maturity of more than 18 months, the issuer shall create a debentureredemption reserve and appoint a debenture trustee to protect the interest ofdebentureholders.

Thusthequalityoftheissueisdemonstratedbytrackrecord/appraisalbyapprovedfinancialinstitutions/creditrating/subscriptionbyQIBs.

PRICINGOFISSUES

The Controller of Capital Issues Act governed issue of capital prior to May 27, 19921947. Under the Act, the premium was fixed as per the valuation guidelines issued.The guidelines provided for fixation of a fair price on the basis of the net asset valueper share on the expanded equity base taking into account, the fresh capital and theprofitearningcapacity.

The repealing of the Capital Issue Control Act resulted in an era of free pricing ofsecurities. Issuers and merchant bankers fixed the offer prices. Pricing of the publicissuehastobecarriedoutaccordingtotheguidelinesissuedbySEBI.

At Premium: Companies are permitted to price their issues at premium in the caseofthefollowing:

- Firstissueofnewcompaniessetupbyexistingcompanieswiththetrackrecord.
- First issue of existing private/closely held or other existing unlisted companieswiththree-yeartrackrecordofconsistentprofitability.
- Firstpublicissuebyexitingprivate/closelyheldorotherexistingunlistedcompanies withoutthree-yeartrackrecordbutpromotedbyexistingcompanieswithafive-yeartrackrecordofconsistentprofitability.
- Existingprivate/closelyheldorotherexistingunlistedcompanywiththree-yeartrackrecordofconsistentprofitability,seekingdisinvestmentsbyofferstopublic withoutissuingfreshcapital(disinvestments).
- Public issue by existing listed companies with the last three years of dividendpayingtrackrecord.

At Par Value: In certain cases companies are not permitted to fix their issue pricesatpremium.Thepricesoftheshareshouldbeatpar.Theyarefor:

- First public issue by existing private, closely held or other existing unlistedcompanieswithoutthree-yeartrackrecordofconsistentprofitabilityand
- Existing private/closely held and other unlisted companies without three-yeartrack record of consistent profitability seeking disinvestments offer to publicwithoutissuingfreshcapital(disinvestments).

FIXEDVERSUSBOOKBUILDINGISSUES

Themaindifferencebetweenofferofsharesthroughbookbuildingandofferofsharesthroughnormalpublicissuecanbeidentifiedonthefollowingparameters:

- ***Price*** at which securities will be allotted is not known in case of offer of sharesthrough Book Building while in case of offer of shares through normal publicissue, priceisknown in advance to investor. Under Book Building, investorsbid for shares at the floor price or above and after the closure of the bookbuildingprocessthepriceisdeterminedforallotmentofshares.

- In case of Book Building, the ***demand*** can be known everyday as the book isbeing built. But in case of the public issue the demand is known at the close oftheissue.

Indian companies are permitted to raise foreign currency resources through twomainsources:

- IssueofForeignCurrencyConvertibleBonds(FCCBs)
- Issue of Ordinary equity shares through depository receipts, namely, GlobalDepository Receipts/ American Depository Receipts to foreign investor's i.e.institutionalinvestorsorinvestorsresidingabroad.

A Depository Receipt (DR) is any negotiable instrument in the form of a certificatedenominated in US dollars. The certificate is issued by an overseas depository bankagainst certain underlying stocks/shares. The shares are deposited by the issuingcompany with the depository bank. The depository bank in turn tenders DRs to theinvestors. A DR represents a particular bunch of shares on which the receipt holderhastherighttoreceivedividend,otherpaymentsandbenefitswhichcompanyannounces from time to time for the shareholders. However, it is non-voting equityholding. DRs facilitate cross border trading and settlement, minimize transactioncost and broaden the potential base, especially among institutional investors.
MoreandmoreIndiancompaniesareraisingmoneythroughADRsandGDRsthesedays.

WHATAREADRsORGDRs?

American Depositary Receipts (ADRs) are securities offered by non-US companieswho want to list on any of the US exchange. Each ADR represents a certain numberof a company's regular shares. These are deposited in a custodial account in the US.ADRs allow US investors to buy shares of these companies without the costs ofinvesting directly in a foreign stock exchange. ADRs are issued by an approved NewYorkbankortrustcompanyagainstthedepositoftheoriginalshares.Whentransactions are made, the ADRs change hands, not the certificates. This eliminatestheactualtransferofstockcertificatesbetweentheUSandforeigncountries.

Global Depositary Receipts (GDRs) are negotiable certificate held in the bank of onecountryrepresentingaspecificnumberofsharesofastocktradedontheexchangeof another country. This is a financial instrument used by the companies to raisecapital in either dollars or Euros. GDRs are also called European Depositary Receipt.ThesearemainlytradedinEuropeancountriesandparticularlyinLondon.

However,ADRsandGDRsmakeiteasierforindividualstoinvestinforeigncompanies,duetothewidespreadavailabilityofpriceinformation,lowertransactioncosts,andtimelydividenddistributions.

WHYDOCOMPANIESGOFORADRsORGDRs?

Indian companies need capital from time to time to expand their business. If anyforeigninvestorwantstoinvestinanyIndiancompany,theyfollowtwomainstrategies. Either the foreign investors can buy the shares in Indian equity marketsortheIndianfirmscanlisttheirsharesabroadinordertomaketheseshareavailabletoforeigners.

But the foreign investors often find it very difficult to invest in India due to poormarket design of the equity market. Here, they have to pay hefty transaction costs.This is an obvious motivation for Indian firms to bypass the incompetent Indianequity market mechanisms and go for the well-functioning overseas equity markets.WhentheyissuesharesinformsofADRsorGDRs,theirsharescommandedahigherpriceovertheirpricesontheIndianbourses.

Anotherproblemfacedbytheforeigninvestorsisrestrictionsonequityownershipby foreigners. Only foreign institutional investors can buy shares in India whereas incaseofADRsorGDRs,anyonecanbuythis.FIIsfacerestrictionsofceilingsorstakesin Indian companies. In contrast, there is no such restriction on GDRs or ADRs, andhenceGDRsorADRsgenerallyenjoyapremium.

WHICHINDIANCOMPANIESARELISTEDABROAD?

Infosys Technologies was the first Indian company to be listed on NASDAQ in 1999.However,thefirstIndianfirmtoissuesponsoredGDRorADRwasRelianceindustries Limited. Beside, these two companies there are several other Indian firmsare also listed in the overseas bourses. These are Satyam Computer, Wipro, MTNL,VSNL,StateBankofIndia,TataMotors,DrReddy'sLab,Ranbaxy,Larsen&Toubro,ITC,ICICIBank,Hindalco,HDFCBankandBajajAuto.

WHATARETHEPRICESOFINDIANADRs&GDRs?

The ADR and GDR prices of the Indian companies are much higher compared to thepricesontheIndianbourses.While,Infosystradesat$72.14atNASDAQ,itquotesat Rs 2,245 on the BSE. Satyam at $24.25, Wipro at $21.50, Tata Motors at $10.20,MTNLat$6.34,DrReddy'sLabat$16.27,HDFCBankat$41.94,BajajAutoat $28.14, RIL at $24.83 and ITC at $35.30 were all quoting at a higher price than theirIndianpeers.

HOWTOTRADEINADRs?

ADRs can be traded either by trading existing ADRs or purchasing the shares in theissuer's home market and having new ADRs created, based upon availability andmarketconditions.

When tradingin existingADRs, the tradeisexecuted on thesecondary market onthe New York Stock Exchange (NYSE) through Depository Trust Company (DTC)without involvement from foreign brokers or custodians. The process of buying new,issued ADRsgoesthroughUSbrokers,Helsinki Exchanges and DTC aswell asDeutscheBank.

WHATARETHENORMSFORINDIANADRsANDGDRs?

TherearenoceilingsoninvestmentinADRsorGDRs.Anapplicantcompanyseekingthe government's approval in this regard should have a consistent good track recordfor a minimum period of 3 years. This condition can be relaxed for infrastructureprojects such as power generation, telecomm, petroleum exploration and refining,ports,airportsandroads.

There is no restriction on the number of GDRs or ADRs to be floated by a companyor a group of companies in a financial year. The government has also relaxed theconversion and re-conversion (i.e. two-way conversion or fungibility) of shares ofIndiancompaniesintodepositoryreceiptslistedinforeignbourses.

The companies have been allowed to invest 100 per cent of the proceeds of ADR orGDR issues for acquisitions of foreign companies and direct investments in jointventures.

ALLOTMENTOFSHARES

PROHIBITIONOFALLOTMENTUNLESSMINIMUMSUBSCRIPTIONRECEIVED

- A company's offer to the public for subscription of equity shares cannot beallotted unless the minimum amount is subscribed for. This minimum amountisdecidedbytheBoardofDirectors,whichaccordingtothemmustberaisedb y the issue of share capital in order to provide for the specific objective asmentionedintheprospectusandwhichhasbeensubscribedbythepublicfor.
- The amount payable on application on each share cannot be less than five percentofthenominalamountoftheshare.
- All money received from applicants for issue of shares is kept deposited in aSchedule Bank until the certificate to commence business is obtained by thecompany. Where such certificate has already been obtained, the deposits arekept until the company has received the entire amount payable on applicationsforsharesuptominimumsubscription.
- Ontheexpiryof120daysaftertheissueoftheprospectus,iftheaboveconditions are not complied with, all money received from applicants has to berepaid without interest. Incase money is not repaid within 130 days after theissue of the prospectus, directors of the company is held responsible to repaythat money with interest at the rate of 6% per annum from the expiry of the130thday.
- The above conditions do not apply to any allotment of shares made subsequenttothefirstallotmentofsharebythecompanytothepublic.

PROHIBITIONOFALLOTMENTINCERTAINCASESUNLESSSTATEMENTINLIEUOFP ROSPECTUSDELIVEREDTOREGISTRAR

- If a company having a share capital did not issue a prospectus or has issued aprospectus but has not proceeded to allot any of the shares offered to the publicfor subscription, cannot allot any of its shares or debentures unless at least 3days before the first allotment of either shares or debentures it has delivered astatement in lieu of prospectus signed by all director in writing to the Registrarforregistration.
- Thisprohibitionofallotmentdoesnotapplytoaprivatecompany.
- If this statement in lieu of prospectus delivered to the Registrar includes anyuntrue statement, then the person authorizing the delivery is held responsibleand is liable for punishment. This is a punishable offence with imprisonmentfor a term up to 2 years or with fine which may be up to the extend of 50000 orwithboth.

EFFECTOFIRREGULARALLOTMENT

- Anallotmentmadebyacompanytoanapplicantshallbe void able at theinstanceoftheapplicant–(a)withintwomonthsafterthe holding of thestatutorymeetingofthecompany,andnotlateror;(b) in case where thecompany is not required tohold a statutory meeting or where the allotment ismadeaftertheholdingofthestatutory meeting, within two months after thedateoftheallotmentandnotlater.
- If any director of a company is responsible of willful contravention of any of theprovisionsofallotment,heisliabletocompensatethecompanyandtheallotteesfo ranylossincurredthereby.Providedanysuchproceedingstorecoverlossesisnotcom mencedaftertheexpirationoftwoyearsfromthedateoftheallotment.

APPLICATIONSFOR,ANDALLOTMENTOF,SHARESANDDEBENTURES

- Theapplicationsforallotmentofshareordebenturesofacompany,donethrough a prospectus issue, is not done until the beginning of the 5thday aftertheprospectusisfirstissuedoranytimelaterasspecifiedintheprospectus.
- The validity of an allotment is not affected by any contravention of the abovepoint,butintheeventofanysuchcontravention,everyofficerofthecompanyis held responsible and subject to a punishment of fine up to the extend ofRs.50000.
- An application for shares or debentures of a company made through issue of aprospectus is generally not revocable until after the expiration of the 5thdayaftertheopeningofthesubscription.

ALLOTMENTOFSHARESANDDEBENTURESTOBEDEALTINONSTOCKEXCHANGE

- Everycompanyintendingtooffersharesordebenturestothepublicforsubscription by the issue of a prospectus shall, before making such issue isrequired to make an application to one or more recognized stock exchanges forseeking permission to list the shares and debentures such issued on the stockexchanges.Whereanappealagainstthedecisionofanyrecognizedstockexchan ge refusing permission for the shares or debentures to be listed on thestock exchange has been preferred, such allotment shall not be void until thedismissaloftheappeal.
- Where the permission has not been applied, the company will repay all moneyreceived from applicants without interest, and if, any such money is not repaidwithin 8 days after the company becomes liable to repay it, the directors areheld responsible. From the expiry of 8thday, they will be jointly liable to repaythat money with interest, not less than 4% and not more than 15%, dependinguponthelengthof theperiodof delayinmakingtherepaymentof suchmoney.
- AllmoneyreceivedasaforesaidshallbekeptinaseparatebankaccountmaintainedwithaScheduledBank,andifdefaultismadeincomplyingwiththeconditionsaforesaid,theneveryofficerofthecompanyisheldresponsibleandthisoffenseispunishablewithfinewhichmayextendto 50000rupees.Moneystandingtothecreditoftheseparatebankaccount,shallnotbeutilizedforanypurposeotherthanthefollowingpurposes,namely–(a)adjustmentagainstallotmentofshares,wheretheshares havebeenpermittedtobe listedonthestockexchangesasspecifiedintheprospectus;or(b) repayment ofmoneyreceivedfromapplicants,wheresharashavenotbeenpermittedtobelistedonthestockexchangesasspecifiedintheprospectus.
- No prospectus shall state that application has been made for permission for theshares or debentures offered thereby to be listed on any stock exchange, unlessitisrecognizedstockexchange.

RETURNASTOALLOTMENTS

Wheneveracompanyhavingasharecapitalmakesanyallotmentofitsshares,thecompanyshall,within30daysthereafter:

- FilewiththeRegistrar areturnoftheallotments,statingthe numberandnominalamountofthesharescomprisedintheallotment,the names,addresses and occupations of the allottees, and the amount, if any, paid or dueandpayableoneachshares.

- Inthecaseofshares(notbeingbonusshares)allottedasfullyorpartlypaid-up, is produced for inspection and examination of the Registrar in the form of acontract constituting the title of the allottee to the allotment together with anycontractof saleor servicesor other consideration in respectof whichthatallotmentwasmade.Thiscontractisdulystamped andfiled withtheRegistrar.
- Inthecaseofbonussharesareturnstatingthenumberandnominalamountofsuchsharescomprisedintheallotmentandthenames,addressesandoccupationsoftheallotteesandacopyoftheresolutionauthorizingtheissueofsuchsharesisfiledwiththeRegistrar.
- In the case of issue of shares at a discount, a copy of the resolution passed bythe company authorizing such issue together with a copy of the order of theTribunalsanctioningtheissueandwherethemaximumrateofdiscountexceeds10%,acopyoftheorderoftheCentralGovernmentpermittingtheissueatthehigherpercentageisfiledwiththeRegistrar.
- Ifdefaultismadeincomplyingwiththeconditionsaforesaid,everyofficerofthecompanyisheldresponsibleandthisoffenseispunishablewithfine,whichmayextendto5000rupeesforeverydayduringwhichthedefaultcontinues.
- No aforesaid conditions will apply to the issue and allotment of shares by acompany, which under the provisions of its articles were forfeited for non-paymentofcalls.

BASISOFALLOTMENT

According to SEBI regulation, the allocation of shares is done under proportionateallotment method. The allotment for each category is inversely proportional to theover subscription ratio. The applications will be categorized according to the numberof shares applied for. The allocation is done by proportionate basis. If the allocationto a applicant works out to be more than hundred but is not a multiple of hundred,the number excess of hundred and fifty would be rounded off to the higher multipleof 100 i.e. 200. If it were 148 then, it would be rounded off to 100. If the sharesallocated on a proportionate basis to any category are more than the shares allottedto applications in that category, the balance share allotment shall be first adjustedagainstanyothercategorywheretheallotmentofsharesarenotsufficientforproportionate allotment in that category. The balance shares, if any remaining aftersuch adjustment will be added to the category comprising of applicants applying forminimumnumberofshares.

ALLOTMENTMETHOD

Totalnumberofapplicantsinthecategoryof100s =2000Tot
alnumberofsharesappliedfor =2,00,000
Numberoftimesoversubscribed =5Propo
rtionateallotmenttothatcategory(2,00,000×1/5) =40,000
Sincetheallotmenthastobemadeinmarketablelots,100shareswillbeallottedto400people.

ILLUSTRATION

Basis of Allocation – Reliance Petroleum Limited ***(Incorporated under the Companies Act,1956onOctober24,2005)***

IssueDetail:Issueof135,00,00,000equitysharesofRs.10eachforcashatapriceofRs.60pe requityshare(IncludingasharepremiumofRs.50perequityshare) aggregatingtoRs.81,000millionincludingpromotercontributionof90,00,00,000equitysharesofRs.10eachforcashatapriceofRs.60pershare(“PromoterContribution”)andthenetissue topublic of 45,00,00,000 equity shares of Rs.10each(“NetIssue”). The netissue will constitute 10% of the fully diluted post issuepaid up capital of Reliance Petroleum Limited (“Company” or “Issuer”). The face valueperequityshareisRs.10.TheissuepriceperequityshareisRs.60anditis6timesofthefacevalue.

The issue was made through the 100% Book Building Process where at least 60% ofthe Net Issue was to be allocated on proportionate basis to Qualified InstitutionalBuyers (“QIBs”) (including 5% of the QIB portion that was to specifically be allottedto mutual funds on proportionate basis). Further, not less than 10% of the Net Issuewas available for allocation on proportionate basis to Non-Institutional Bidders andnotlessthan30%oftheNetIssuewasavailableforallocationonproportionatebasistoRetailBidders,subjecttovalidbidsbeingreceivedatorabovetheIssuePrice.

TheIssuereceived21,08,279applicationsfor23,04,97,33,824equitysharesresulting in 51.22 times subscription. The details of the applications received in theIssue from Qualified Institutional Buyers, Non-Institutional and Retail IndividualInvestorscategoriesareasunder(*Beforetechnicalrejections*):

Category	No.ofApplications	No.ofShares	Subscription
Retail Bidders	2094659	2011656932	14.90
NonInstitutionalBidders	13209	2622131892	58.27
QualifiedInstitutionalBidders	411	18415945000	68.20

FinalDemand:Thefinaldemandatdifferentbidpricesisasunder:

BidPrice	No.ofShares	%toTotal	CumulativeTotal	Cumulative% toTotal
57	3493900	0.02	23087276300	100.00
58	1031800	0.00	23083782400	99.98
59	107000	0.00	23082750600	99.98
60	34334100	0.15	23082643600	99.98
61	2020200	0.01	23048309500	99.83
62&CutOff	23046289300	99.82	23046289300	99.82
	23087276300	**100.00**		

The Basis of Allocation was finalized in consultation with Bombay Stock ExchangeLimited on May 3, 2006. The Committee of Directors of the Company at its Meetingheld at Hyderabad on May 3, 2006 has approved the following Basis of Allocation ofsharesoftheIssueandhasallottedthesharestothesuccessfulapplicants.

Allocation to Retail Investors: The category was subscribed 13.80 times. The totalnumber of shares allotted in this category is 13,50,00,000 equity shares and thenumber of allottees is 1247592. The category-wise details of the Basis of Allocation(*Sample*)areasunder:

Category	No.ofApplications	%to Total	TotalNo. ofSharesApplied	%to Total	No.of SharesAllocated	Ratio	TotalNo.ofSharesAllocated
100	74871	3.86	7487100	0.40	100	5:69	542500
200	100887	5.20	20177400	1.08	100	10:69	1462100
300	67209	3.47	20162700	1.08	100	15:69	1461100
400	64367	3.32	25746800	1.38	100	20:69	1865700
500	189368	9.76	94684000	5.08	100	25:69	6861200
600	45310	2.34	27186000	1.46	100	3:7	1941900
700	34686	1.79	24280200	1.30	100	1:2	1734300
800	562408	29.00	449926400	24.14	100	40:69	32603400

900	5022	0.26	4519800	0.24	100	5:8	313900
1000	115074	5.93	115074000	6.17	100	55:76	8327700
1100	8673	0.45	9540300	0.51	100	11:14	681500
1200	10712	0.55	12854400	0.69	100	6:7	918200
1300	3446	0.18	4479800	0.24	100	14:15	321600
1400	3440	0.18	4816000	0.26	101	FIRM	347440
		ADDITIONAL			100	9:16	1944
1500	32200	1.66	48300000	2.59	109	FIRM	3509800
1600	621601	32.05	994561600	53.36	116	FIRM	72105716

AllocationtoNonInstitutionalInvestors: The category was subscribed 57.59times. The total number of shares allotted in this category is 450,00,000 equityshares and the number of allottees is 7328. The category-wise details of the Basis ofAllocation(*Sample*)areasunder:

Category	No.ofApplications	%to Total	TotalNo. ofSharesApplied	%to Total	No.of SharesAllocated	Ratio	TotalNo.ofSharesAllocated
1700	299	3.41	508300	0.02	100	3:10	9000
1800	71	0.81	127800	0.00	100	1:3	2400
10000	416	4.75	4160000	0.16	174	FIRM	72384
50000	137	1.56	6850000	0.26	868	FIRM	118916
100000	177	2.02	17700000	0.68	1736	FIRM	307272
120000	7	0.08	840000	0.03	2083	FIRM	14581
150000	48	0.55	7200000	0.28	2604	FIRM	124992
200000	50	0.57	10000000	0.39	3472	FIRM	173600
500000	48	0.55	24000000	0.93	8681	FIRM	416688
1000000	15	0.17	15000000	0.58	17362	FIRM	260430
1500000	6	0.07	9000000	0.35	26044	FIRM	156264
2000000	6	0.07	12000000	0.46	34725	FIRM	208350
4000000	6	0.07	24000000	0.93	69450	FIRM	416700
5000000	1	0.01	5000000	0.19	86812	FIRM	86812
11300000	1	0.01	11300000	0.44	196195	FIRM	196195
32258000	2	0.02	64516000	2.49	560077	FIRM	1120154
93540000	1	0.01	93540000	3.61	1624080	FIRM	1624080
111290000	1	0.01	111290000	4.29	1932244	FIRM	1932244

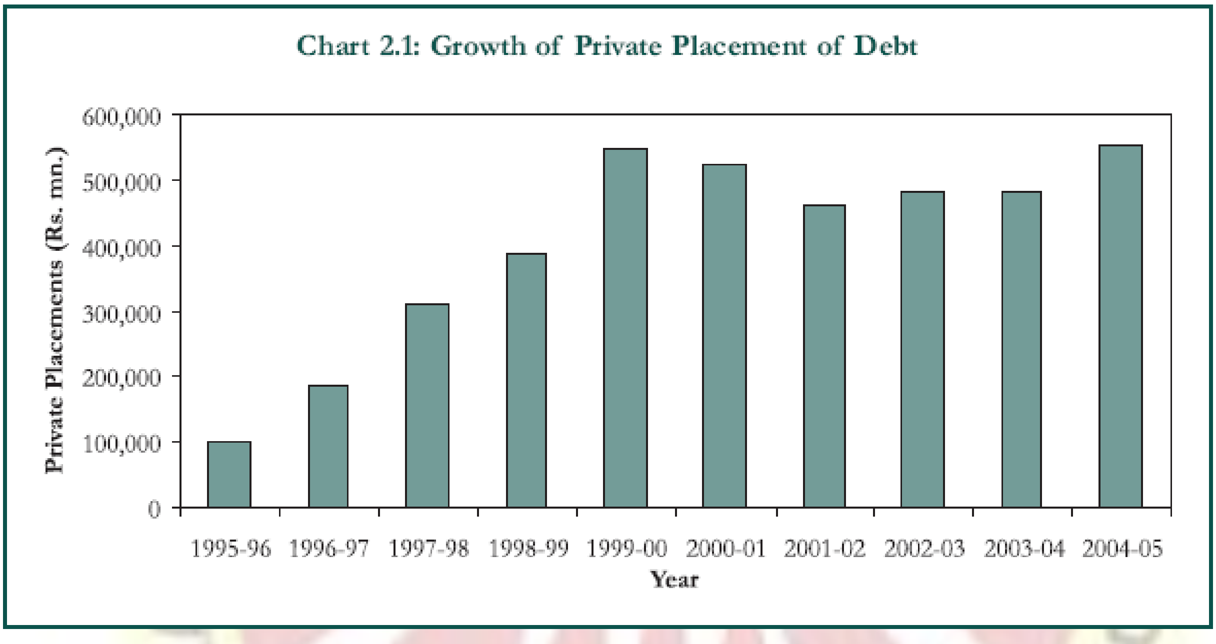
Allocation to QIBs: The category was subscribed 68.20 times. Allocations to QIBshave been done on a proportionate basis. As per the SEBI guidelines, Mutual Fundswereinitiallyallotted5%ofthequantumofsharesavailable(135,00,000)onproportionate basis and other QIBs and unsatisfied demands of Mutual Funds wereallotted the remaining available shares (2565,00,000) on proportionate basis. Thesectoral cap and other limits applicable to the holding of shares in company havebeen taken intoaccount while allotting shares. Mutual Funds were allotted 11.51%forQIBsegmentandotherQIBapplicantswereallotted88.49%ofthesharesforQIB segment.Thetotalnumberofallotteesis411.

Category	No.ofShares
FIs/Banks	15861666
MFs	31072909
FIIs	216366000
VC	17714
InsuranceCompanies	6681711
Total	**270000000**

PRIVATEPLACEMENT

Theprivateplacementinvolvesissueofsecurities,debtorequity,toselectedsubscribers, such as banks, FIs, MFs and high net worth individuals. It is arrangedthrough amerchant/investment banker, who acts as an agent of the issuer andbrings together the issuer and the investor(s). Since these securities are allotted to afewsophisticatedandexperiencedinvestors,thestringentpublicdisclosureregulationsandregistrationrequirementsarerelaxed.TheCompaniesAct,1956, states that an offer of securities to more than 50 persons is deemed to be publicissue.

In sharp contrast to a shrinking public issues market for corporate securities, thelast few years have witnessed huge resource mobilization through private placement.AccordingtoPrimeDatabaseestimates, atotalof114issuers(institutionalandcorporate)raisedRs.5,51,838millionthrough319privatelyplacedissuesin2004-05. 176 issues out of 319 were made by the government sector units, which togethermobilized 82% of the total. The amount raised through the private placement of debtissueshavebeenonanincreasingtrendoverthepastfewyears(Chart2.1).



Mostly, debt securities were privately placed. Though, there were some instances ofprivate placements of equity shares, there is no comprehensive data coverage of this.The two sources of information regarding private placement market in India arePrime Database and RBI. The former data set, however, pertains exclusively to debtissues.RBIdata,whichiscompiledfrominformationgatheredfromarrangers,covers equity private placements also. RBI estimates the share of equity in total privateplacements as rather insignificant. Some idea, however, can be derived from theequity shares issued by NSE-listed companies on private placement basis. A total of96 companies privately placed equities mobilizing around Rs.58,982 million during2004-05.

Of the 319 debt private placements, 176 (55%) were from the government/bankingsector that together mobilized 82% of the total amount mobilized. The All IndiaFinancialInstitutions(AIFIs)&Bankscontinuedtotopthelistwith59%(Rs.326,522 million), followed by the Private Sector Undertakings with 18% share (Rs.101,910million). The top '10' issuers accounted for 53.9% of total private placement during2004-05.

Table:Issuer-wiseDistributionofPrivatePlacementofDebt

	ssueAmount(Rs. mn.)		%ofIssueAmount	
Issuer	**2003-04**	**2004-05**	**2003-04**	**2004-05**
AllIndiaFinancialInstitutions/Banks	253,088	326,522	52.26	59.17
StateFinancialInstitutions	42,084	23,808	8.69	4.31

PublicSectorUndertakings	58,809	64,412	12.14	11.67
StateLevelUndertakings	65,642	35,186	13.55	6.38
PrivateSector	64,656	101,910	13.35	18.47
Total	**484,279**	**551,838**	**100.00**	**100.00**

Source:PrimeDatabase

Sectoral distribution shows that the banking and financial services continued todominate the private placement market, raising 64% in 2004-05 followed by powersector,whichaccountedfor16%duringtheyear.

Table:SectoralDistributionofResourcesMobilizedbyPrivatePlacement

(In percent)

		2004-05
Financial&Banking	76	64
Power	17	16
WaterResources	5	2
Telecommunications	1	2
Others	1	10
Total	**100**	**100**

Source:PrimeDatabase

The maturity profile of issues in the private placement market ranged between 12months to 204 months during 2004-05. The largest number of placements was for36 months (87 placements) and 60 months (57 placements). A total of 78 offers hadaputoption,while83offershadacalloption.

Unlike public issues of bonds, it is not mandatory for corporate issuing bonds in theprivateplacementmarkettoobtainanddisclosecreditratingfromanapprovedcreditratingagency.Ratingis,however,requiredforlisting.Ofthe319debtprivateplacementdeals during2004-05,297issues(93%)wentforratingand22didnotgetrated.

Private placement accounted for 68.4% of total resources mobilized by the corporatesector from the primary market. The corresponding share of public issues was ameager26.6%.

Table:ResourcesRaisedbyCorporateSector

(AmountinRs.mn.)

Year	Public Equity Issues	DebtIssues			Total	Share(%)ofPrivate Placementin		Share (%) ofDebt inTotalResourceMobilization(5/6*100)
		Public Issues	PrivatePlacements*	Total (3+4)	Mobilization (2+5)	TotalDebt (4/5*100)	TotalResourceMobilization (4/6*100)	
1	2	3	4	5	6	7	8	9
1995-96	88,820	29,400	100,350	129,750	218,570	77.34	45.91	59.36
1996-97	46,710	69,770	183,910	253,680	300,390	72.50	61.22	84.45
1997-98	11,320	19,290	309,830	329,120	340,450	94.14	91.01	96.67
1998-99	5,040	74,070	387,480	461,550	466,580	83.95	83.05	98.92
1999-00	29,750	46,980	547,010	593,990	623,740	92.09	87.70	95.23
2000-01	24,790	41,390	524,335	565,725	590,520	92.68	88.79	95.80
2001-02	10,820	53,410	462,200	515,610	526,430	89.64	87.80	97.94
2002-03	10,390	46,930	484,236	531,166	541,556	91.16	89.42	98.08
2003-04	178,210	43,240	484,279	527,519	705,729	91.80	68.62	74.75
2004-05	214,320	40,950	551,838	592,788	807,108	93.09	68.37	73.45

*Datafrom2000-01onwardsincludeonlyissueswithatenorandput/calloptionof1yearormore,whiledataforearlieryearsincludeallprivatelyplaceddebtissuesirrespectiveoftenor.
*Source:*PrimeDatabase

Unit-IV

MUTUAL FUNDS

Mutual funds are investment companies that use the funds from investors to investinothercompaniesorinvestmentalternatives.Theyhavetheadvantageofprofessional management, diversification, convenience and special services such ascheque writing and telephone account service. It is generally easy to sell mutual fundshares/unitsalthoughyouruntheriskofneedingtosellandbeingforcedtotakethe price offered. Mutual funds come in various types, allowing you to choose thosefundswithobjectives,whichmostcloselymatchyourownpersonalinvestmentobjectives. A load mutual fund is one that has sales charge or commission attached.Thefeeisapercentageoftheinitialinvestment.Generally,mutualfundssoldthrough brokers are load funds while funds sold directly to the public are no-load orlow-load. As an investor, you need to decide whether you want to take the time toresearchprospectivemutualfundsyourselforpaythecommissionandhaveabrokerwho willdothatforyou.Allfundshaveannualmanagementfeesattached.

MutualFundSchemesmaybeclassifiedontheBasisofitsStructureanditsInvestmentObjective.LetusfirstdiscusstheclassificationbyStructure:

Open-EndedMutualFunds

Anopen-endedmutualfundistheonewhoseunitscanbefreelysoldandrepurchased by theinvestors. Such funds arenot listed on bourses since the AssetManagement Companies (AMCs) provide the facility for buyback of units from unit-holders either at the NAV, or NAV-linked prices. Instant liquidity is the USP of open-endedfunds:youcaninvest in or redeem your units at will in a matter of 2-3 days.In the event of volatilemarkets, open-ended fundsarealsosuitablefor investmentappreciationintheshort-term.Thisishowtheywork:ifyouexpecttheinterestratestofall,youparkyourmoneyinanopen-endeddebtfund.Then,whenthepricesoftheunderlyingsecuritiesrise,leadingtoanappreciation in your fund's NAV, youmake a killing by selling it off. On the other hand, if you expect the Bombay StockExchangeSensitivityIndex–theSensex–togainintheshortterm,youcanpickuptherightopen-endedequityfundwhoseportfoliohasscripslikelytogainfromtherally,andsellitoffonceitsNAVgoesup.

INVESTMENT OBJECTIVES

HowSuitableAreOpen-EndedFunds forAnIncreaseInMyInvestment? Open-ended equity funds are, indeed, suitable for an increase or appreciation in yourinvestment.Again,yourchoiceinanequityfundcanvary,dependingonyourappetite for risk. Sector specific funds like Infotech/Technology or Pharma fundsinvest only in companies of that particular sector, and are more risky. At the sametime, if the scrips of a particular sector are doing well, the returns from investing inansectorspecificmutualfundmayprovetobeworththerisk.

AreOpen-EndedMutual Funds Suitable For Regular Income? An open-endeddebt fund is best suited for income. Debt funds generally give you an option ofreceivingdividendonamonthly,quarterly,half-yearlyoronannualbasis.

ToWhatExtentDoOpen-Ended Funds Protect Me Against Inflation? Open-Ended Mutual Funds provide a fair amount of protection against inflation. But fundswith an equity portfolio – growth funds – provide better protection than debt fundsbecause equities, over the long term, provide the best means of beating inflation.Moreover,long-termcapitalgainsaretaxexempted.

Can I Borrow Against Open-Ended Mutual Funds? There are some banks thatoffer loans against your mutual funds. Different banks have their own criteria onwhichtheyapprovetheloans.

RISK CONSIDERATIONS

HowAssuredCanIBeOfGettingMyFullInvestmentBack?Youcannot becompletely sure of getting your full investment back. It depends on the quality andthe kind of portfolio you invest in. In fact, in an equity fund, there are no guaranteesat all since the fund trades in the secondary markets, and a crash there could resultin a major part of your investment coming to nothing. However, in debt funds, thecredit ratings of the constituents of the portfolio are a good indicator to how safe thefund, and, thus, your principal amount are. For instance, if the portfolio consists ofmostlygovernmentsecurities,itisthesafest.

How Assured Is My Income? It again depends on the quality of the portfolio of themutual fund you invest in. The returns from your fund are related to the market. Inthe simplest sense if the stock market or the debt market is performing well you canexpect to receive a good return over your investment in the fund. Some funds giveyou a dividend or growth option. Also, income is more assured in case of debt fundsascomparedtoequityfunds.

Are There Any Risks Unique To Investing In An Open-Ended Fund? Since Open-Ended Mutual Funds invest in scrips in the secondary market, volatility in theirportfolio reflects on the returns. An open-end fund may be subject to inflows at onetime or suddenredemptions, whichleads toaspurtor afallin the NAV, thusaffecting your returns. Also, the value of the scrips in the portfolio can fluctuate duetovariousmarketforces,thusaffectingthereturnsofthefund.

Are Open-Ended Mutual Funds rated for their credit quality? Open-ended equityfunds are not credit rated. However, the holdings of debt funds are. The portfolio listof debt funds provides the details of all the instruments held by the fund and theirrespectivecreditratings.

BUYING,SELLING,ANDHOLDING

HowDoIBuyAnOpen-EndedFund?Units of Mutual Funds can be purchasedthrough investment service centres of the Asset Management Company (AMC) orthrough the distributors. Also some AMC offer units through NSE Brokers also. ThepriceperunitofamutualfundislinkedtotheNetAssetValue(NAV)ofthefund.

WhatIsTheMinimumInvestment And The Range Of Investment For Open-Ended Mutual Funds? Minimum investment in an open-ended mutual fund variesbetween Rs.500 and Rs.5,000. Some open-ended funds charge an entry load, i.e., asales charge, expressed as a percentage of the NAV, is deducted from the amountinvested. Also, the AMC gives you the option to invest through SIP. In SystematicInvestmentPlanyouinvestafixedportioneveryfixedperiodtotakeadvantageo ftheconceptofrupeecostaveragingwhereyoubuymoreunitswhenthepricesaredown and less units when the prices rule high. This reduces your average cost of purchaseoftheunits.

WhatIsTheDurationOfOpen-EndedMutualFunds?Open-ended funds, bydefinition,havenotimeduration.Theycanbepurchasedorredeemedatanytime.

CanOpen-Ended Mutual Funds Be Traded InThe Secondary Market?No, open-ended mutual funds cannot be sold or purchased in the secondary market. They aredirectly repurchased by the AMC. However, they can be bought from certain brokerswhodealinthem.

What Is The Liquidity Of Open-Ended Mutual Funds? Open-ended funds provideinstantliquidityasmutualfundsredeemunitsdaily,eitheratNAV,oratNAVplusa small exit load. There is a concept of Contingent Deferred Sales Charge where theexit load is charged only if the redemption takes place before a specified time periodor above a specified amount. A majority of open-ended mutual funds allow switchingamong the various funds of the same AMC without any load. You generally get yourredemptionrequestsprocessedpromptly,andreceivethechequein3-4days.However, in case of Equity Linked Savings Schemes (ELSS) there is a lock in periodofthreeyears.

HowIsTheMarket Value Of Open-Ended Mutual Funds Determined, And HowDoIKeepTrackOf It? Although the units of open-ended mutual funds are nottraded in the secondary market, their sale and repurchase price is a function of theNAV of the fund. If the value of the portfolio of the fund rises, so will the NAV and,hence, the market value of the open-ended mutual fund. Thus, the NAV is the mostimportantinformationaninvestormustseek.Andthisinformationisavailablethrough newspapers where it is given daily, the AMC themselves, the Internet, andalso through the periodic mails that your AMC is supposed to send you. So you canjudgethemarketvalueofyourinvestmentbytrackingthemovementoftheNAV.

WhatIsThe Mode of Holding Open-Ended Mutual Funds? When you subscribetoanopen-endedmutualfund,youreceiveanaccountstatementstatingyourownership of the number of units in the mutual fund. Thereafter, you get an accountstatement for every transaction you make. In some cases, certificates are also issued.Your AMC may give you the option of holding the certificates in the physical form, oryoucanreceivethesecertificatesinthedematerialized(demat)form,i.e.,thecertificates are not physically issued to you; instead, they are credited to your demataccount.

TAXIMPLICATIONS

EquityFund	***DebtFund***
ShortTermTax–10%	ShortTermTax–10%
LongTermTax–NIL	LongTermTax–20%

IncomereceivedfromMutualFunds,accordingtothelatestBudgetproposalsdividends from Mutual Funds will not be taxed in the hands of the investor. Beforethe new proposals, dividend from debt funds was subject to a 10 per cent dividenddistribution tax plus surcharge. Dividends received from open-ended equity fundswerecompletelytax-free.

Capitalgainstax:The difference between the sale consideration and the cost ofacquisition of the asset is called capital gain. If the investor sells his units and earnscapital gains he is liable to pay capital gains tax. Capital gains are of two types:Short-termandLong-termcapitalgains.

Short Term Capital Gains; If the units are held for a period of less than one yeartheywillbetreatedasshort-termcapitalgainsandtheinvestorwillbetaxeddependingontheincometaxrateapplicable tohim.

LongTermCapitalGains; All units held for a period of more than 12 months willbe classified as long-term capital assets. The investor has to pay long-term capitalgains on the units held by him for period of more than 12 months. In this case theinvestorofadebtfundwill

- Pay tax at a flat rate of 10 % (plus surcharge of the applicable tax rate) on thecapitalgainswithoutindexationor
- Avail cost indexation on capital gains and pay 20 % tax (plus surcharge of theapplicabletaxrate)whicheverislower.

Indexationmeansthatthepurchasepriceismarkedupbyaninflationindexresultinginlowercapitalgainsandhencelowertax.

Inflationindexfor theyear
oftransferInflationindex=
....
Inflation indexfortheyearofacquisition

Close-EndedMutualFunds

Closed-ended mutual funds have afixed number of units, and a fixed tenure (3, 5,10, or 15 years), after which their units are redeemed or they are made open-ended.These funds have various objectives: generating steady income by investing in debtinstruments, capital appreciation by investing in equities, or both by making anequalallocationofthecorpusindebtandequityinstruments.

INVESTMENT OBJECTIVES

HowSuitableare Closed-EndedFundsForanIncrease inMy Investment? Sinceunits of closed-ended funds rise and fall in the market like any other stock, they arewell suited for an increase in your investment. However, a mutual fund is moreinfluenced by the value of its own portfolio than any other factor. Units of an equityfund are more frequently traded than a debt fund. Also, the NAV of an equity fundrises and falls at a much faster pace. On the other hand, an equity fund provideshealthyappreciationinNAVinthelongterm.

AreClosed-Ended MutualFunds Suitable For Regular Income? Closed-endeddebt funds, with their conservative investment approach, are best suited for income.Thesefundsdeclaredividendannuallyorsemi-annually

ToWhatExtentDo Closed-Ended Funds Protect Me Against Inflation? Withstocks being better than bonds in providing returns on a long-term basis, an equityclosed-ended fund is better equipped to guard your investment against inflation inthelongrun.

CanIBorrowAgainstClosed-Ended Mutual Funds? No, if you require liquiditythere is an option of selling these closed-ended mutual fund's units in the secondarymarket.

	MorganStanleyGrowthFund
AMC	MorganStanleyInvestmentManagementPvt.Ltd.

Fund	Morgan Stanley MutualFund	**Category**	Equity-Diversified
Scheme Plan	Growth	**SchemeType**	**Closed Ended**

NAVChart(ThreeYears)

RISK CONSIDERATIONS

HowAssuredCanIBeOfGettingMyFullInvestmentBack?Youcannot becompletely sure of getting your full investment back. Depending on their investmentobjectiveandunderlyingportfolio,closed-endedfundscanbeveryvolatileorbefairlystable.Hence,yourprincipalisnotassured.

How Assured Is My Income? It depends on the portfolio of your closed-ended fund.A portfolio of debt instruments or shares of some blue-chip companies may provideregulardividends.

AreThereanyRisksUniquetoInvestinginaClosed-EndFund? The value of aclosed-end mutual fund can fluctuate drastically. So, your units can trade at a heftydiscount to their NAV, thus depriving you from realizing the true value of your units.Thisisbecausealthoughclosed-endedfundsare,generally,listed,thereisnoliquidity.Investorsmustbuyafundifitsportfolioisgood;unitsaretradingatagooddiscount,andthestockmarketispoisedtorise.

AreClosed-EndedMutualFundsratedfortheir credit quality? Closed-endfunds are not rated. However, it is important to note that the holdings of a debt fundaregenerallyrated,andthisservesasanindicatorofthesafetyoftheportfolio.

BUYING,SELLING,ANDHOLDING

How Do I Buy a Closed-Ended Fund? Closed-ended funds tap the market with theirinitial offers. Alternatively, if the funds are listed, the units can also be picked upfromthesecondarymarket.

WhatisTheMinimumInvestmentAndThe Range Of Investment for Closed-Ended Mutual Funds? Minimum investment in closed-ended mutual funds varies,and normally ranges between Rs.2,000 and Rs.5,000. There is no maximum limit ofinvestment.

WhatisTheDurationOfClosed-EndedMutualFunds? A closed-end fund is,typically, a five-year fund. However, the duration period may vary between 3 and 15years.

CanClosed-EndedMutualFundsbetradedintheSecondaryMarket?Yes,closed-ended funds are listed on the stock exchanges and, thus, can be traded in thesecondary market. However, the liquidity of closed-ended funds is poor, and theytradeonaheftydiscounttotheirNAVinthesecondarymarket.

Whatis The Liquidityof Closed-Ended Mutual Funds? The Indian stock marketslack depth and, thus, the closed-ended mutual funds are illiquid where they arelisted and trade with a heavy discount to their NAVs. Besides listing, some mutualfundsalsoofferrepurchaseoptionsintheirclosed-endedfundsataNAV-linkedpriceafteracertainlock-inperiod.

HowistheMarket Value of Closed-Ended Mutual Funds Determined, and HowdoI Keep Track of It? The market price of a closed-ended fund is a direct functionofitsNAV.ThehighertheNAV,thehigherthemarketpriceandvice-versa.However,unitsofaclosed-endedfundalwaystradeatadiscounttotheirNAV.Forinstance,iftheNAVofafundisRs.13, unitsmaybetradingataroundRs.11.However,unitsof assured return funds are an exception. Their unit price on the bourses does notchasetheNAV;itchasestheassuredreturn.TheNAVisthemostimportantinformation an investor must seek while investing in a closed-ended mutual fund.And this information is available through various newspapers, the AMC themselves,the Internet, and also through the periodic mails which your AMC is supposed tosendtoyou.

What is The Mode of Holding Closed-Ended Mutual Funds? When you subscribetoaclosed-endedmutualfund,youreceiveeitherphysicalcertificates,ortheaccountnumberiftheyareheldinthedematform.

TAXIMPLICATIONS

Whiledividendpaidonclosed-endedmutualfundsisfullytaxexempt,onredemptionor sale of units in the secondary market, your realization will attract short-termcapital gains tax of 10 per cent. However, you can save tax by investing in Equity-LinkedSavingsScheme(ELSS)underSection88oftheIncomeTaxAct,1961,according to which 20 per cent of the amount invested in ELSS which have a lock-inperiod of 3 years-can be deducted from your tax liability subject to a maximuminvestment of Rs.10,000 per year. Also available under Section 88 are two pensionplans:UnitTrustofIndia'sRetirementBenefitUnitPlan(RBP)andKothariPioneer'sPensionPlan.

IntervalFunds

Interval funds combine the features of open-ended and close-ended schemes. Theyare open for sale or redemption during pre-determined intervals at NAV relatedprices.

LetusnowclassifyMutualFundSchemesontheBasisofitsInvestmentObjective:

GrowthFunds

The aim of growth funds is to provide capital appreciation over the medium to long-term.Suchschemesnormallyinvestamajorityoftheircorpusinequities.Ithas beenproventhatreturnsfromstocks,haveoutperformedmostotherkindofinvestmentsh eldoverthelongterm.Growthschemesareidealforinvestorshavingalong-termoutlookseekinggrowthoveraperiodoftime.

IncomeFunds

The aim of income funds is to provide regular and steady income to investors. Suchschemesgenerallyinvestinfixedincomesecuritiessuchasbonds,corporatedebentur es and Government securities. Income Funds are ideal for capital stabilityandregularincome.

BalancedFunds

The aim of balanced funds is to provide both growth and regular income. Suchschemesperiodicallydistributeapartoftheirearningandinvestbothinequitiesandfi xedincomesecuritiesintheproportionindicatedintheirofferdocuments.Ina rising stock market, the NAV of these schemes may not normally keep pace, or fallequallywhenthemarketfalls.Theseareidealforinvestorslookingforacombinationofi ncomeandmoderategrowth.

MoneyMarketFunds

The aim of money market funds is to provide easy liquidity, preservation of capitalandmoderateincome.Theseschemesgenerallyinvestinsafershort-terminstruments such as treasury bills, certificates of deposit, commercial paper andinter-bank call money. Returns on these schemes may fluctuate depending upon theinterest rates prevailing in the market. These are ideal for Corporate and individualinvestorsasameanstoparktheirsurplusfundsforshortperiods.

LoadFunds

A Load Fund is one that charges a commission for entry or exit. That is, each timeyou buy or sell units in the fund, a commission will be payable. Typically entry andexit loads range from 1% to 2%. It could be worth paying the load, if the fund has agood performance history. The maximum load – as specified by SEBI, entry and exitputtogetheris7%oftheNAV.

No-LoadFunds

A No-Load Fund is one that does not charge a commission for entry or exit. That is,nocommissionispayableonpurchaseorsaleofunitsinthefund.Theadvantageofanoloa dfundisthattheentirecorpusisputtowork.

WecanfurtherclassifyMutualFundSchemesontheBasisofspecialty:

IndustrySpecificSchemes

IndustrySpecificSchemesinvestonlyintheindustriesspecifiedintheofferdocument.The investmentofthesefundsislimitedtospecificindustrieslikeInfoTech,FMCG,Pharmaceu ticalsetc.

IndexSchemes

IndexFundsattempttoreplicatetheperformanceofaparticularindexsuchastheBSESensexortheNSENifty.

SectoralSchemes

SectoralFundsarethose,whichinvestexclusivelyinaspecifiedindustryoragroup of industriesorvarioussegmentssuchas‘A’Group sharesorinitialpublicofferings.