CHAPTER 1

GLOBAL FINANCIAL MARKETS

LEARNING OUTCOMES

After going through the chapter student shall be able to understand:

- Introduction to Global Financial Market
- Role of Financial Market in Economic Development of a country
- Stakeholders in Financial Market (Domestic and Global)
- Indian Financial Market Scenario

1. INTRODUCTION TO GLOBAL FINANCIAL MARKETS

As per the encyclopedia (http://www.bankpedia.org), the International Financial Market is the place where financial wealth is traded between individuals (and between countries). It can be seen as a wide set of rules governing various institutions where assets are traded between those in surplus to those in deficit.

The financial market comprises the markets (stock market, bond market, currency market, derivatives market, commodity market and money market), the institutions which work in them with different aims and functions (Central Bank, Ministry of Economy and Finance, Monte Titoli, BorsaItaliana and CONSOB), as well as direct/indirect policies orientated to making the market the place (not only a physical place but also an electronic or online place) where the exchange between surplus and deficit units is carried out as efficiently as possible.

1.1 International Capital Market

NASDAQ

NASDAQ is the largest US electronic stock market in terms of shares traded and is home to leading companies across all industry sectors, such as Microsoft, Intel, Google, Oracle, Nokia, K-Swiss, Carlsberg, Starbucks and Staples. Over the past decade, it has listed far more companies than any other exchange. Although it made its initial reputation as a growth company exchange, NASDAQ today offers a market tier with arguably the highest listing standards—the NASDAQ Global Select Market—to provide a platform for mature, blue-chip companies.

The world's first electronic stock market, NASDAQ has strived to maintain its reputation as the leader in exchange technology—it offers trading speed of less than one millisecond and trades more shares than any other US exchange. The exchange has made client services another key point of differentiation and has developed a number of offerings to assist listed companies with investor relations, equity research, risk management, corporate governance and other post-listing needs. NASDAQ also considers its listing cost structure to be a competitive advantage. It has actively pursued the opportunities created by the globalization of equity capital markets. Its benchmark indices have been traded since 1999 and are licensed in 37 countries.

New York Stock Exchange (NYSE Euronext)

The NYSE Euronext positions itself as the global leader among exchanges. The world's largest and most liquid equities marketplace, the exchange looks to maintain its brand image as the "gold standard," both in terms of listing standards and the blue-chip companies it hosts. Like all the major exchanges, NYSEEuronext has been challenged in recent years by the maturing of national exchanges from Mumbai to Milan that can now tap large local pools of capital to accommodate large offerings and have the infrastructure to support the swelling numbers of initial public offerings generated by global economic growth. To be able to participate in the growth of listings outside the United States, the NYSE made a merger proposal to the Euronext stock exchange valued in the neighborhood of US$10 billion in June 2005.

The merger, which was approved by Euronext shareholders and became effective in the first quarter of 2007, gives the new NYSE Euronext greater geographic and product diversification. The marriage of the NYSE and Euronext creates the world's first intercontinental market, with a combined value of listed companies of about €21 trillion (US$26 trillion). The resulting new exchange covers more time zones than any other and will trade in two of the world's main currencies, dollars and euros, making it easier for investors to trade securities listed on any of the seven constituent exchanges of the new group. Furthering its goal of globalization, the NYSE Euronext announced a strategic alliance with the Tokyo Stock Exchange in January 2007.

London Stock Exchange

London Stock Exchange plc (the "LSE") is central to maintaining London as one of the leading international financial centres. The LSE's shares were themselves listed on the London Stock Exchange in July 2001. As on 30 October 2014, there were nearly 1,900 companies traded on the LSE's market for listed securities (the "Main Market") and nearly 1,130 listed on the AIM market - a second market designed for those smaller or growing companies which may not satisfy all the requirements for admission to the Main Market. Of the companies traded on the Main Market, around 600 were international, drawn from nearly 60 countries including Canada, Poland, Egypt and India. As these figures indicate, being on the Main Market gives the individual company, large or small, access to a large pool of capital with a global dimension and provides a market on which its shares can be widely traded. This allows a company to raise capital to develop its business and, for the company's original investors, it provides an opportunity to spread or dilute their risk. Obtaining access to this pool of capital by listing on the Main Market can also significantly raise the profile and prestige of a company, both nationally and internationally.

Singapore Stock Exchange

Singapore Exchange (SGX) is the Asian Gateway, connecting investors in search of Asian growth to corporate issuers in search of global capital. SGX represents the premier access point for managing Asian capital and investment exposure, and is Asia's most international exchange with more than 40% of companies listed on SGX originating outside of Singapore.

SGX offers its clients the world's biggest offshore market for Asian equity futures, centered on Asia's three largest economies – China, India and Japan. In addition to offering a fully integrated value chain from trading and clearing, to settlement and depository services, SGX is also Asia's pioneering central clearing house. Headquartered in Asia's most globalized city, and centered within the AAA strength and stability of Singapore's island nation, SGX is a leading Asian counterparty for the clearing of financial and commodity products.

Luxembourg Stock Exchange

The Luxembourg Stock Exchange is a stock exchange based in Luxembourg City, in southern Luxembourg. The Luxembourg Stock Exchange is a world-class player offering an attractive international listing marketplace for a large range of securities. With more than 3,000 listed issuers coming from over 100 countries, the Luxembourg Stock Exchange meets capital market players' needs as a result of an 80-year old experience, high-quality products and services as well as fast, customer-oriented and secure processes. A broad range of instruments are admitted for trading on the Luxembourg Stock Exchange. A majority revolves around debt securities, investment funds, warrants, GDRs and equities.

Hongkong Stock Exchange

Hongkong Stock Exchange (HKEx) is a leading global operator of exchanges and clearing houses based in Hong Kong, Asia's premier international financial center, and one of the world's largest exchange groups by market capitalization.

HKEx operates the securities and derivatives markets and their related clearing houses and is the frontline regulator of listed companies in Hong Kong. It also owns the London Metal Exchange (LME) in the UK, the world's premier base metals market.

In Hong Kong, HKEx regulates listed issuers and administers listing, trading and clearing rules. It also provides services, primarily at the wholesale level, to participants and users of its Exchanges and Clearing Houses, including issuers and intermediaries (such as investment banks or sponsors, securities and derivatives brokers, custodian banks and information vendors) which service investors directly. These services comprise trading, clearing and settlement, deposit and nominee services and information services across multiple products and asset classes.

1.2 International Commodity Market

Major international commodity exchanges of the world are briefly discussed as below:

Chicago Mercantile Exchange (CME): It is a financial and commodity derivatives trading platform which has its headquarter in Chicago. It was established in 1898 as the Chicago Butter and Egg Board. Presently, Chicago offers contract of all kinds which includes agriculture, credit, equity index, interest rates and other futures/options investments.

Chicago Board of Trade (CBOT): It is formed in 1848 and being considered among oldest future/options trading exchanges in the world. The exchange offers more than 50 different futures and option contracts for investors which scattered over a number of asset classes.

New York Mercantile Exchange (NYMEX): The NYMEX is the world's largest physical commodity futures exchange, which offers a wide variety of products. Commodity Exchange Inc. (COMEX) which acts as a division of the NYMEX also offers exposure to various metals contracts.

London Metal Exchange (LME): LME was established in 1877. However, it has its roots in 1571, when the Royal Exchange in London was founded, trading only copper at that time. It is a major exchange which offers exposure to futures and options of a various varieties of base metals and other commodity products. Some of the metals which have been traded include aluminium, copper, tin, nickel, zinc, and lead..

Intercontinental Exchange Inc. (ICE):

The Intercontinental Exchange is an American company which operates futures and over-the-counter contracts through internet. In the beginning, the company was operating energy contracts but has increased its scope by offering exposure to a number of commodities including cocoa, cotton, sugar, iron ore, natural gas and crude products.

2. ROLE OF FINANCIAL MARKET IN ECONOMIC DEVELOPMENT OF A COUNTRY

Efficient and sound financial market of a country plays an important role in the nation's economic development. The economic development of a country depends upon the mobilization of savings and the flow of these savings to the corporates. The corporates acquires funds by issuing securities in the financial market by influencing the investors to invest their savings or borrowing from financial institutions. The savings of individuals, corporate sector and government should be mobilized by the financial institution, through financial markets by creating financial instruments with the help of the watchful eyes of financial regulators. The role of various financial markets in the economic development of a country is discussed as follows:

(i) Capital Market

Capital market plays an important role in a country's industrial growth. Capital market is the market where long term debt and equity funds are traded. Industries which require capital on a large scale may tap the capital market. Therefore, the capital market provides the much needed liquidity into the economy and it gives a big boost to the GDP of an economy as it serves as an effective source of allocation of capital to the Industry and Government.

The primary role of capital market is to transfer surplus funds to deficit sectors which are in dire need of money. The capital market performs the crucial function of facilitating capital formation in the economy. Capital market can be divided into primary market and secondary market. Primary market is utilized by companies for the purpose of setting up new businesses or for expanding or modernizing the existing business. Secondary market provides an opportunity to the company to raise the market price of their shares, thereby enabling them to attract more capital from investors and loans from banks. It also helps the shareholders to increase their wealth.

However, the contribution of Medium and Small Scale (MSME) in India's GDP cannot be denied. As per details provided by the Press Information Bureau dated 22nd July, 2014, the estimated contribution of manufacturing sector Micro, Small and Medium Enterprises (MSME) to GDP, during 2012-13, is approximately 7.04%. However, taking into account the contribution of services sector MSME, which is estimated at 30.50% during 2012-13, the share of MSME sector in GDP of the country, during 2012-13, is 37.54%. It has also been observed that MSME sector that provides the highest number of employment opportunities has been hit by severe capital crunch. So, this is an area where immediate measures are required so that necessary capital can be infused to provide much needed liquidity. This is urgent because unless the MSME sector will get the much needed capital they deserve, they cannot boost up their production. If production doesn't get increased, employment generation will not take place. Low employment generation will not raise the standard of living of the people. This will slow the rate of economic growth and development of an economy. The SME Exchange is a welcome move for the Small and Medium Scale Enterprises, but it is alone not enough to revive MSME.

Global Scenario in Capital Market

Globally, major trends in the capital market revolve around the effect of continuous evolving of regulations after the 2008 crisis and the consequences of new emerging technologies such as block chain and robotic process automation (RPA).Capital Market firms are increasingly adopting RPA to reduce cost. It will also help them to overcome competitors.

Blockchain is being already deployed to remove inefficiencies in the current international capital market structure. Private securities blockchain solution will enable the capital market firms to create digital assets for private securities which will help in direct and immediate access by regulatory bodies. Further, block chain will enable almost instant settlement of transactions and automation of back offices of banks and unshackle billions of collaterals that act as insurance for trading.

(ii) Money Market

Money market is the market where short-term funds are traded. In simple term, it means that all the financial assets or instruments which can be easily converted into money are traded in this market. The short-term money requirement of the borrowers can be easily met with the funds provided by the money market.

Money markets play a key role in banks' liquidity management and the monetary policy of RBI. Though the discussion has been taken place keeping RBI in mind, the intricacies explained in the following paragraphs apply to international scenarios as well. Also, recent international trends in the money market have been highlighted at the end.

(a) Banks' liquidity management

Banks have to maintain Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR). CRR is the reserve which the Banks have to keep with Reserve Bank of India (RBI). On the other hand, SLR is the amount which the banks have to keep with themselves. Banks are often evaluated on the basis of their liquidity, or their ability to meet cash and collateral obligations without incurring substantial losses.SLR requirements help banks to do that. Whenever the RBI issues treasury bills on behalf of the Government, CRR and SLR requirements of banks are automatically met.

(b) Monetary policy

Monetary policy affects rates of interest, inflation and business cycle. Government through the introduction of repos and reverse repos tweak the rate of interest, thus, reducing or increasing money supply by impacting inflation, thereby effecting changes in business cycles. Also, by introducing treasury bills and other money market instruments, it affects money supply and consequently inflation and business cycles.

In normal times, money markets are among the most liquid in the financial sector. By providing the appropriate instruments for liquidity trading, the money market allows the refinancing of short and medium-term positions and facilitates the mitigation of one's business liquidity risk with the help of commercial papers, commercial bills and certificate of deposits.

Global Scenario in Money Market

Lots of regulatory reforms have been initiated globally with primarily the focus on USA. Here, the Basel III norms have discouraged the banks to accept deposits and pay interest thereon. As a result, liquidity investors are flocking to money market as a short term liquidity tool. However, new rules regarding commercial paper have put the investors in the money market in a cautious mood.

Further, yield on 99% of all sovereign debts in Europe is negative.The current focus is on monetary easing, with the European Central Bank (ECB) along with the central banks of Sweden, Switzerland

and Denmark have earmarked unconventional policy such as negative interest rates and quantitative easing (QE).

(iii) Foreign Exchange Market

Foreign exchange earned through foreign direct investment in India can be used to remove the poverty and other productive purposes. Inflow of foreign exchange increases the scale of production and national income of the country. With the rise in the demand of domestic goods, resources of a country are fully utilized and it helps in reducing the unemployment in a country.

Foreign exchange (forex) markets provide traders with a lot of flexibility. This is because there is no restriction on the amount of money that can be used for trading. Forex markets provide traders with a wide variety of trading options. They have the choice of entering into spot trade or they could enter into a future agreement. Futures agreements are also available in different sizes and with different maturities to meet the needs of the Forex traders. Therefore, Forex market provides an option for every budget and every investor with a different appetite for risk taking.

Further, the Forex market is transparent in comparison to other financial market as it is huge in size and operates across several time zones. Information regarding Forex markets is easily available. Also, it is almost impossible to rig prices in the foreign exchange market for an extended period of time.

Global Scenario in Foreign Exchange Market

Globally, the interbank market is a network of banks that trade currencies with each other. Banks also engage in the SWIFT market. It allows them to transfer foreign exchange to each other. SWIFT stands for Society for World-Wide Interbank Financial Telecommunications.

In the retail market, the Chicago Mercantile Exchange was the first to offer currency trading. It launched the International Monetary Market in 1971. Other trading platforms include OANDA, Forex Capital Markets, LLC and Forex.com.The retail market has more traders than the Interbank Market. But the total dollar amount traded is less. The retail market doesn't influence exchange rates as much. (Source: "The Foreign Exchange Market," Martin Boileau, University of Colorado.)

Central banks don't regularly trade currencies in foreign exchange markets. But they have a significant influence. Central banks hold billions in foreign exchange reserves. Japan holds a huge amount mostly in U.S. dollars. Japanese companies receive dollars in payment for exports. They exchange them for yen to pay their workers.

Japan, like other central banks, could trade yen for dollars in the forex market when it wants the value to fall. That makes Japanese exports cheaper. Japan prefers to use more indirect methods though, such as raising or lowering interest rate to affect the yen's value. (Source: "The Main Players in the Forex Market," FXStreet.com.)

On the other hand, the Federal Reserve in USA announced that it would raise interest rates in 2014. That sent the dollar's value up 15 percent.

Recent trends

Earlier, on an average $6 trillion of foreign exchange changes hands on a particular day. However, it may never return as industry observers say, as tighter bank regulation, declining market and slowdown in world growth and trade has been taking its toll in the foreign exchange market.

Trading desks at some of the biggest banks in London and New York -- the largest centers in foreign exchange -- are grappling with lower volumes in actively traded currencies like the yen, Swiss franc and Australian dollar.

(iv) Derivative market

The derivatives market is the financial market for derivatives, financial instruments like futures, contracts or options, which are derived from other forms of assets. Since all transactions related to derivatives take place in future, it provides individuals with better opportunities because an individual who want to short (sell) some stock for long time can do it only in futures or options hence the biggest benefit of this is that it gives numerous options to an investor or trader to execute all sorts of strategies.

Global Scenario in Derivatives Market

The United States was home to the first wave of equity options exchange foundations in the 1970s. A second wave of new derivatives exchanges occurred in the 1980s and early 1990s in Europe. During that time a financial derivatives exchange was established in almost every major Western European financial market – the most important ones being London with Liffe in 1982, Paris with Matif in 1986, and Frankfurt with DTB in 1990. Most of these organizations formed their own clearing houses. In recent years, new derivatives exchanges have started to compete with existing derivatives marketplaces. For instance, ISE commenced trading in 2000 and became the market leader in US equity options trading together with CBOE in 2003. In 2004, BOX successfully entered US equity options trading.

3. STAKEHOLDERS IN FINANCIAL MARKET (DOMESTIC AND GLOBAL)

Various stakeholders in the financial market can be categorized into following four segments:

(i) Primary stakeholders in financial market

- Shareholders
- Lenders
- Companies
- Mutual fund Organizations/holders/fund managers

(ii) Service providers in financial market

- Merchant Bankers

- Brokers
- Underwriters
- Depositories
- Custodians

(iii) Regulators in financial market

- Securities and Exchange Board of India (SEBI)
- Reserve Bank of India
- Insurance Regulatory and Development Authority of India (IRDAI)
- Pension Fund Regulatory and Development Authority (PFRDA)

(iv) Administrators to facilitate the financial market

- Association of Mutual funds of India (AMFI)
- Foreign Exchange Dealers Association of India (FEDAI)
- Fixed Income Money Market and Derivative Association of India (FIMMDA)
- Association of Investment Bankers of India (AIBI)

(i) Primary stakeholders in financial market

(a) Shareholders

In simple language, shareholders are the owners of a company. So, a shareholder is any person such as an individual, company or other institution who hold at least one share out of company's total shares. As shareholders are owners of the company they get benefit when the share prices increase. In the same way, the shareholders lose out when the company's shares plummet.

The shareholders participate in the financial market (secondary market) by buying and selling shares. Their actions depend upon which way the market is behaving. If the market price is low, they tend to buy more shares. On the other hand, if the market price of shares is high, they will sell more shares to book profit. Thus, they provide the much needed liquidity in the stock market.

(b) Lenders

A lender in relation to a financial market is either a company or any other form of corporation that issues bonds or debentures to make its end meet. Funds are available to another with the expectation that the funds will be repaid, in addition to any interest and/or fees, either in increments or as a lump sum. They also provide the much needed liquidity in the financial market by facilitating the flow of funds from deficit spending to surplus spending sectors.

(c) Corporates

Corporates raise money either through the share market route or through the bond market route. Raising money by issuing shares to the public generally helps the companies to amass huge amount of capital. It keeps the financial market ticking by enabling mobilization and allocation of saving from the people, be it, individual investors, companies and institutional investors whether foreign or domestic.

However, raising of equity share capital has its repercussions. Cost of equity share capital is costly. Moreover, companies have to meet a lot of regulatory compliances at the time of initial public offerings which takes a lot of time, energy and money. But, if the company managed to keep its share prices on the higher side, it will easily get more funds in the future whether through equity or debt. If the company opting to raise funds through the debt route, it has certain advantages and disadvantages. The benefits are lower cost of capital in comparison to equity. The debt route also tends to increase the earning per share (EPS) of the company which consequently leads to escalation of share prices of the company. And, the demerit is that a debt has to be repaid alongwith interest. So, too much of debt may lead an organization to financial/default risks and may land it in financial distress.

(d) Mutual fund Organizations

A mutual fund is a financial institution or intermediary that pools the savings of investors for collective investment in a diversified portfolio of securities. A fund is 'mutual' as all of its returns, minus its expenses, are shared by fund's investors. A mutual fund serves as a link between the investor and the securities market by mobilizing savings from the investor and investing them in the securities market to generate returns.

(ii) Service providers in financial market

(a) Merchant Bankers

As per the Securities and Exchange Board of India (Merchant Banker) Regulations, 1992, merchant banker means any person who is engaged in the business of issue management, either by making arrangements regarding selling, buying, or subscribing to securities, or acting as a manager, consultant, or advisor, or rendering corporate-advisory services in relation to such issue management. It is mandatory to appoint a merchant banker in case of a public issue. The functions of merchant banker includes – submitting offer documents to SEBI, due diligence i.e. certifying that all the disclosures made in the draft prospectus or letter of offer are true and fair and will enable the investors to make an informed decision etc.

Globally, merchant banker plays more or less the same role as discussed above. Some of the top Merchant Bankers in USA are Merrill lynch, Citigroup, Goldman Sachs, J.P. Morgan and Morgan Stanley. They provide services to top companies in the world. For example, Morgan Stanley has been responsible for hundreds of technology financing and M&A transactions aggregating over $500 billion in value. Further, Goldman Sachs has served all the big names in tech, including Microsoft, Apple, Facebook, Twitter, Ebay and Alibaba.

(b) Brokers

Stock Brokers are individuals who participate in the stock market on behalf of clients. They buy and sell shares on behalf of the clients on their instructions. In order to actively participate in the capital market, they should be SEBI registered. So, they facilitate trading in the stock market (secondary market) by undertaking buy and sell transactions on behalf of the client.

In USA, most "brokers" must be registered with the Securities Exchange Commission (SEC) and join a "self-regulatory organization," or SRO. Globally, margin financing is popular, in which, many large broking houses provide financing facilities to clients who borrow money to invest in stocks. Therefore, Stock exchanges monitor the extent to which brokers are lending in line with their net worth.

(c) Underwriters

Underwriters are those persons who assume the risk of others. In capital market, in case of new issues, they assume risk by guaranteeing that in case the shares are not subscribed fully by the public, the unsubscribed portion will be subscribed by the underwriter itself. They do it by charging a small fee.

So, how do the underwriters make profit? They buy the shares of the company before they are actually listed on a stock exchange. The underwriters make their profit on the difference in price between what they paid before the IPO and when the shares are actually offered to the public.

(d) Depositories

Depository is an institution which maintains investors account in electronic form. One of the main functions of the Depository is to transfer the ownership of shares from one investor to another whenever the trading of shares takes place. It helps in reducing the paper work involved in trade, expedites the transfer and reduces the risk associated with physical shares such as damage, theft, and subsequent misuse of the certificates or fake securities.

There are two types of depositories in India which are known as NSDL (National Securities Depository Limited) and CSDL (Central Depository Services (India) Limited). They interface with the investors through their agents called Depository participants (DPs). DPs could be the banks (private, public and foreign), financial institutions or SEBI registered trading members.

Globally, depositories provide the same set of services as has been rendered by CDSL and NSDL.

(e) Custodians

Custodians provide custodial services for safe keeping of securities. Besides safe keeping, they provide other services for a fee (generally 1% of the total volume of transactions) such as physical transfer of share certificates and a trustee of the same but also provides ancillary services such as physical transfer of share certificates, collecting dividends and interest warrants and conforming to transfer regulations. Besides that, it also updates client status on their investment status. Even though securities are in the custody of depositories, the custodians act as a complementary to them by providing various services as mentioned above. In India, The Stock Holding Corporation of India (SHCIL) and the SBI Share Holding Corporation are the leading custodians.

After liberalization in 1991, foreign institutional investors (FIIs) were allowed to invest in the Indian Capital Market. Most of the FII business in India is routed through foreign custodians. According to the US laws, no US fund is allowed to use a custodian that does not have a capital adequacy of USD 200 million. No Indian custodian meets this requirement. Therefore, only foreign banks operate as custodians for US based FIIs, pension funds, and corporates. Hong Kong Bank, Deutsche Bank, Citi Bank, and Standard Chartered Bank are some leading foreign banks which operate as custodians.

(iii) Regulators in financial market

(a) Securities and Exchange Board of India (SEBI)

SEBI was born in 1992. The basic objective was to protect the interest of investors in securities and promotes the development of securities market. The important objectives of SEBI are:

i) Protect the interest of investors in securities.

ii) Promotes the development of securities market.

iii) Regulating the securities market.

Outside India

Securities Exchange Commission (SEC) in USA performs more or less the same functions as given to SEBI. But the stark difference is the amount of penalty. SEC can impose an unlimited amount of fine which SEBI cannot. That is the reason SEC has more teeth in comparison to SEBI and acts as an effective deterrent against malpractices in the stock market.

(b) Reserve Bank of India

The Reserve Bank of India was established in 1935 with the provision of Reserve Bank of India Act, 1934. Though privately owned initially, in 1949 it was nationalized and since then fully owned by Government of India (GoI). The preamble of the Reserve Bank of India describes its main functions as to regulate the issue of Bank Notes and keeping of reserves with a view to securing monetary stability in India and generally to operate the currency and credit system of the country to its advantage.

Outside India

Federal Reserve (Fed) in the USA's policies is primarily driven by growth and employment figures, at the expense of inflation. On the other hand, we have the RBI, whose policies are primarily driven by inflation, at the expense of growth. So which approach is better depends upon the situation of the economy. In the USA and European Union, where rate of interest is very low encourages the industry to borrow at cheaper cost and contributes towards economic development and growth. However, in India, the aim of RBI is to keep the rate of interest high to discourage the industry to borrow large amount of money and consequently to contain inflation.

(c) Insurance Regulatory and Development Authority of India (IRDAI)

IRDA Act was passed in 1999. The main aim of the Insurance Regulatory and Development Authority of India is to protect the interest of holders of Insurance policies to regulate, promote and ensure orderly growth of Insurance industry & for matters connected therewith or incidental thereto. Under this Act, Controller of Insurance under Insurance Act,1938 was replaced by newly established authority called Insurance Regulatory and Development Authority (IRDA).

Outside India

In USA, insurance is almost regulated by the individual state governments. In Canada, Office of the Superintendent of Financial Institutions Canada (OSFI)sets the minimum regulatory requirements and expectations to support policyholder and creditor protection, giving due regard to the need to allow institutions to compete effectively. As healthy companies are in the best position to protect policyholders and creditors, OSFI is aware of the impact of its requirements and expectations on competition domestically and internationally.

Insurance regulators in other jurisdictions pursue similar goals but with different legislative and policy tools and with different economic experiences and conditions. OSFI will consider the pace, scope and impact of reforms when renewing the regulatory framework, to ensure that we are able to incorporate best practices, and limit – to the extent practical – unintended consequences and an uneven playing field. *(Source: Office of the Superintendent of Financial institutions, Canada)*

(d) Pension Fund Regulatory and Development Authority (PFRDA)

To be a model Regulator for promotion and development of an organized pension system to serve the old age income needs of people on a sustainable basis. Pension systems throughout the world have been under close scrutiny over the last couple of decades. Numerous reforms have been carried out to tackle the sustainability and adequacy of pension arrangements in the face of the rising global demographic challenge.

Outside India

The main law which governs the establishment, maintenance, and termination of pension plans in the United States is the Employee Retirement Income Security Act (ERISA).

Prudential supervision of Australian pension funds started in 1993.The objective of the regulation regarding superannuation aimed at reducing the riskiness of superannuation investments, dealing with retirement incomes policy,equal treatment of members and various other matters.

(iv) Administrative authorities to facilitate the financial market

(a) Association of Mutual funds of India (AMFI)

The Association of Mutual Funds in India (AMFI) is dedicated to developing the Indian Mutual Fund Industry on professional, healthy and ethical lines and to enhance and maintain standards in all areas with a view to protecting and promoting the interests of mutual funds and their unit holders.

AMFI, the association of SEBI registered mutual funds in India of all the registered Asset Management Companies, was incorporated on August 22, 1995, as a non-profit organization. As of now, all the 42 Asset Management Companies that are registered with SEBI are its members.

The Mutual Fund Dealers Association of Canada (MFDA) is the national self-regulatory organization (SRO) that oversees mutual fund dealers in Canada.

(b) Foreign Exchange Dealers Association of India (FEDAI)

Foreign Exchange Dealers Association of India (FEDAI) was set up in 1958 as an Association of banks dealing in foreign exchange in India (typically called Authorised Dealers - ADs) as a self-regulatory body and is incorporated under Section 25 of The Companies Act, 1956. It's major activities include framing of rules governing the conduct of inter-bank foreign exchange business among banks vis-à-vis public and liaison with RBI for reforms and development of forex market.

Internationally, forex dealer provides online trading services to allow individuals to speculate on rapidly changing foreign exchange rates. Forex Dealer Members (FDMs) are regulated in the United States by the Commodity Futures Trading Commission (CFTC) and National Futures Association (NFA), as well as by national and local regulatory bodies where they conduct business.

(c) Fixed Income Money Market and Derivative Association of India (FIMMDA)

The Fixed Income Money Market and Derivatives Association of India (FIMMDA), an association of Scheduled Commercial Banks, Public Financial Institutions, Primary Dealers and Insurance Companies was incorporated as a Company under section 25 of the Companies Act, 1956 on June 3rd, 1998. FIMMDA is a voluntary market body for the bond, money and derivatives markets.

FIMMDA has members representing all major institutional segments of the market. The membership includes Nationalized Banks such as State Bank of India, its associate banks and other nationalized banks; Private sector banks such as ICICI Bank, HDFC Bank, IDBI Bank; Foreign Banks such as Bank of America, ABN Amro, Citibank, Financial institutions such as IDFC, EXIM Bank, NABARD, Insurance Companies like Life Insurance Corporation of India (LIC), ICICI Prudential Life Insurance Company, Birla Sun Life Insurance Company and all Primary Dealers.

The International Swaps and Derivatives Association (ISDA) is a trade organization of participants in the market for over-the-counter derivatives. It's headquarter is in New York City, and has created a standardized contract (the *ISDA Master Agreement*) to enter into derivatives transactions.

(d) Association of Investment Bankers of India (AIBI)

In the early 1990s, the merchant banking industry in India witnessed a phenomenal growth with over 1500 merchant bankers registered with SEBI. In order to ensure the wellbeing of the industry and for promoting healthy business practices, it became necessary to set up a Self-Regulatory Organization within the industry. This led to the birth of the Association of Investment Bankers of India (AIBI). AIBI was promoted to exercise overall supervision over its members in the matters of compliance with statutory rules and regulations pertaining to merchant banking and other activities. AIBI was granted recognition by SEBI to set up professional standards, for providing efficient services and to establish standard practices in merchant banking and financial services. AIBI, in consultation with SEBI, is working towards improving the compliance of statutory requirement in a systematic manner.

AIBI's primary objective is to ensure that its members render services to all its constituents within an agreed framework of ethical principles and practices. It also works as a trade body promoting the interests of the industry and of its members. *(Source www.aibi.org.in)*

Internationally, International Association of Investment Bankers (IAIB)since its inception in 1994 has leveraged its collective expertise, best practice knowledge, industry insights, and global reach to assist clients in executing mergers, acquisitions, divestitures, and strategic partnerships.

Its membership is composed of established boutique investment banks from around the world whose primary focus is advising middle market and emerging growth companies. A highly collaborative group, we hold monthly conference calls and gather twice each year to review creative transaction structures and current market dynamics, as well as to share perspectives on important industry issues. Through these efforts, they are able to offer their clients a truly differentiated advisory service that leverages the significant transaction experience and domain expertise of their member firms.

The International Association of Investment Bankers (IAIB) is an affiliation of investment banking firms from Europe, North America, Australia and Asia, working together to broaden their reach and leverage their expertise within the global marketplace.

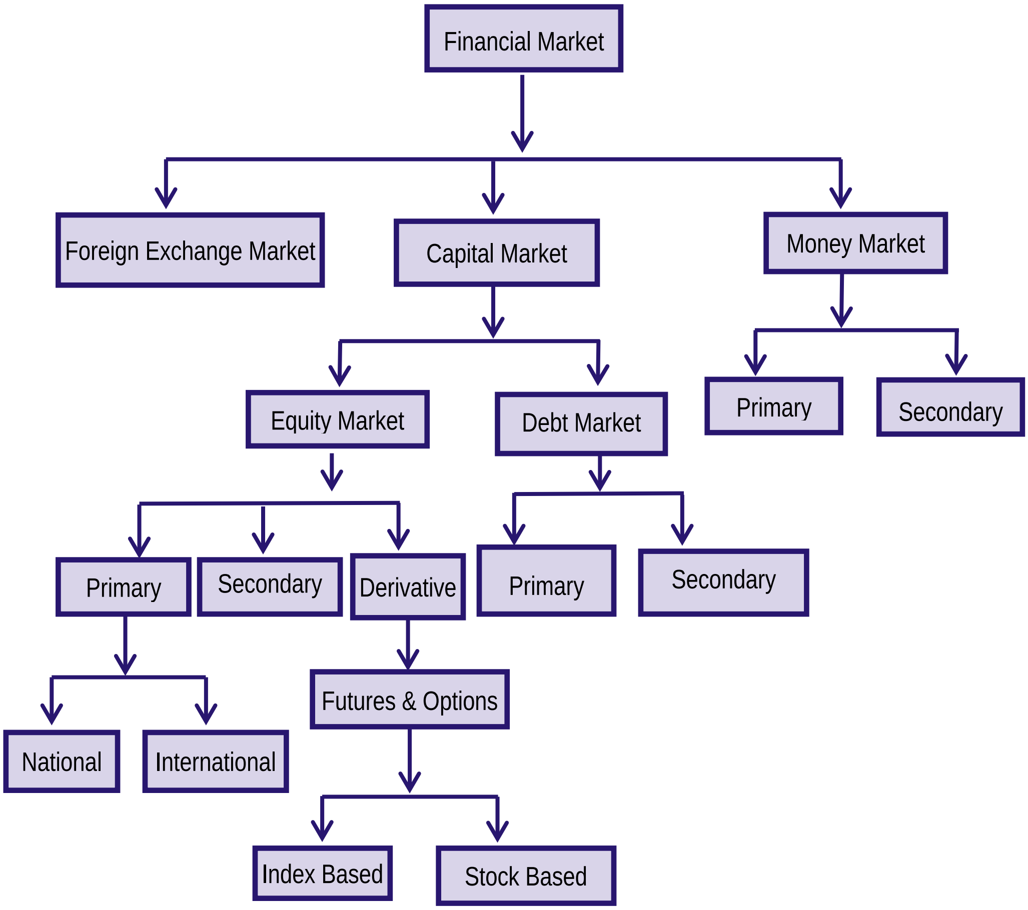
Since 1994, the IAIB member firms have utilized this network to offer their clients worldwide access to providers of capital, advisory services and acquirers and sellers of businesses. With this capability, member firms are able to provide substantial added value to their clients beyond that typically offered by purely domestic advisors. *(Source www.iaib.org)*

4. INDIAN FINANCIAL MARKET SCENARIO

4.1 Introduction to Financial Market

The financial market is a market where trading of securities including equities, bonds, currencies and derivatives takes place. Financial market can be divided into money market and capital market. Money market is a market for short term securities having a maturity period of less than one year. Capital Market is a market for long term securities having a maturity period of more than one year. Further, capital market can be divided into primary market and secondary market. In primary market, securities (shares, bonds, debentures) are issued to the public for the first time. While in secondary market, trading (purchase and sale) takes place in those securities which are already issued to the public.

The financial market has been graphically depicted as follows:



4.2 Functions of Financial Markets:

The main functions of financial markets are enumerated as below:

1) To facilitate creation and allocation of credit and liquidity.

2) To serve as intermediaries for mobilization of savings.

3) To help in the process of balanced economic growth.

4) To provide financial convenience.

5) To provide information and facilitate transactions at low cost.

6) To cater to the various credits needs of the business organizations.