

# Preface

Financial system comprises a set of sub-systems of financial institutions, markets, instruments, services and regulatory bodies. It plays a crucial role in the economic development of any country, which can be viewed on the basis of growth in national and per capita income. An increase in national income signifies the economic growth of a country, which is measured in terms of gross domestic product (GDP) of a country. The growth of GDP in any economy depends upon the increase in the proportion of savings and investment to GDP of a nation. The level and growth of savings, investments and capital formation in an economy are essential for economic growth in the country. Economic growth and development of any country depends upon a sound financial system which facilitates the mobilization of finance. Thus, a sound financial system provides a mechanism by which savings are transformed into investments. It contributes significantly to economic growth of a country by mobilizing excess funds from its surplus sectors to deficit sectors and utilizing these effectively for productive purpose. Basically, credit activities are considered as borrowing and lending activities. The capital-user relationship between borrowers and lenders depends upon the principles of reimbursement. In this backdrop, interest rate is an indispensable leverage and tool in credit activities and controlling market economy. The interest rate, an effective tool of monetary policy of a country, is controlled by the Reserve Bank of India (RBI) as the central bank in India, which may transform the level and structure of interest rates over the period. It ultimately affects the size and density of types of investments, the structural adjustment process, growth, production, unemployment and domestic inflation. Apart from that, interest rate policy affecting and regulating stability of exchange rates is also used as a device for controlling capital flows for an open economy like India. This practically influences the investment and development, the balance of payments and international trade relations of a nation.

However, the financial system and market scenario, both in India and abroad, have undergone a sea change due to globalization and liberalization policies undertaken by the Government in order to promote the growth in different sectors of the economy. Under such a situation, there has been a paradigm shift in the scope of financial system, markets and services. As such, financial system has witnessed a tremendous momentum during the phase of economic reforms to meet the increasing demand of the corporate sectors, which also influences the economic growth in India. Financial system in India is regulated by the independent regulators in banking, insurance, and financial markets. Apart from that, the central government plays the role of regulator in a number of sectors. The regulators ensure that the market participants behave in a desired manner so that the securities markets continue to be a major source of finance for corporate and government while safeguarding the interest of investors effectively. Policy formulation and the regulation of the Indian financial market are made under the guidance of the Ministry of Finance (MOF) and the RBI. While the RBI regulates the money markets, the SEBI regulates and supervises the securities markets, the IRDA regulates the insurance markets.

Because of the tremendous importance of financial system in Indian economy, the subject, 'Indian Financial System and Markets' has been included in the undergraduate and postgraduate courses in commerce, management and finance, and professional courses including CA, CWA, CS, CFA in India. This book has been designed to meet the needs of students pursuing such courses. In fact, the idea of the present work developed out of my Ph.D work in finance. The contents of the book have been class-tested with my students in the Department of Accounting and Finance, St. Xavier's Colloge (Autonomous), Kolkata and Department of Commerce (MBA-Finance), University of Calcutta.

The book has been divided into 13 chapters.

Chapter 1 provides an overview of Indian financial system incorporating the different financial innovations, significance, structure of Indian financial system and role of financial system in economic development in India. A brief outline on evolution and reforms in Indian financial system has also been provided here.

Chapter 2 delves into Indian banking system incorporating the concept of alternative measures to money supply in India and their different components, structure of commercial banking system in India, credit creation process of commercial banks, high powered money and concept of money multiplier. There is a separate section on functions of the RBI, instruments of monetary and credit control and main features of monetary policy adopted in India since independence.

In Chapter 3, important issues relating to concept of development banks, their needs in Indian financial system and difference between commercial banks and development banks have been discussed. A brief outline on major development banks (i.e. IFCI, IDBI, ICICI, EXIM Bank, SIDBI, SFCs, and NABARD) and their functions has also been portrayed here.

Chapter 4 intends to provide a detailed idea on life insurance as well as general insurance business in India and role of LIC as well as GICI in the financial system. The chapter also focuses on mutual funds sectors in India and the role of UTI as a premier mutual fund organization.

Chapter 5 provides a detailed account of interest rate structure in India incorporating conceptual aspects of interest rate, contribution of interest rate in economic progress, its various theories, the term structure, and a sketch on recent changes in interest rate structure in India.

Chapter 6 discusses financial markets in India incorporating reforms measures in money markets, foreign exchange market and capital markets.

In Chapter 7, an endeavour has been made to provide a basic idea on money markets, its structure and a brief outline on major money market instruments in India. A brief introduction on SBI DFHIL, STCIL, and MMMFs has also been given. Money market reforms and its recent trends in India have also been highlighted here.

Chapter 8 portrays the organization and operations of primary capital market in India including various issues of securities, public issue mechanism (*like Fixed Price Method, Book Building Method and Pure Auction Method*), IPO Grading operation as well as Green Shoe Option in public issues. A current trend of primary capital markets has also been incorporated here.

Chapter 9 elaborates on the organization and operations of stock market incorporating different important issues like listing of securities at BSE and NSE, role of market intermediaries, stock exchange trading, depository system, dematerialization and rematerialisation process, trading and settlement of securities, financial derivatives, etc.

Chapter 10 provides an outline of leading Indian stock exchanges (BSE, NSE) and leading stock market indices (Sensex, Nifty) in India.

Chapter 11 comprehensively describes important issues relating to regulatory framework in case of investors' protection, role of market regulators like DEA, DCA, RBI, SEBI, stock exchanges, and IRDA. Surveillance cell in stock exchanges, grievances concerning stock exchange dealings and their removal have also been discussed here. This chapter also includes a brief outline on legislations governing the securities market, role of judiciary and media in investors' protection.

Merchant bankers render various financial services like corporate counselling, project counselling and pre-investment study, credit syndication and project finance, corporate restructuring, capital issue management, underwriting, portfolio management, venture capital financing, etc. Chapter 12 discusses thoroughly the different aspects of the financial services and merchant banking activities in India.

Chapter 13 provides an overview of credit rating as financial services in India comprising the concept, historical background, objectives, the rating process and the rating methodology. A brief outline on the profile and activities of different credit rating agencies in India has been given here. A synopsis on regulatory framework relating to the SEBI (Credit Rating Agencies) Regulations, 1999 has also been incorporated.

Case studies have been incorporated in all chapters of this book to facilitate better understanding of readers. Additional reading material is also available on the companion website:

[www.mhhe.com/sahaifsm](http://www.mhhe.com/sahaifsm)

I am pleased to put on record my best regards to my reverend teachers for their blessings. I owe my gratitude to the learned authors of India and abroad from whose work I have taken so many ideas for my present work. I acknowledge with thanks the guidance given during the discussion on the contemporary issues related to my present study by CEOs of different financial institutions including merchant banking, stock broking firms and others. I extend my best wishes to my all friends and colleagues for their support and cooperation.

No words can express my indebtedness to my parents, whose encouragement and blessings have always been with me in the completion of the present work. My beloved wife is highly supportive and her emotional support during times of my academic stress has helped me to complete the book effectively.

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Suggestions and feedback from readers for improving this book will be highly appreciated. I look forward to receiving them.

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