RECENT TRENDS IN INDIAN CAPITAL MARKET

By
Dr. P. D. OJHA

LALA LAJPATRAI MEMORIAL LECTURES

(Thirteenth Series 1984)

LALA LAJPAT RAI COLLEGE OF COMMERCE AND
ECONOMICS, BOMBAY 400 034

Recent Trends in Indian capital Market

P. D. OJHA

I am grateful to the President, the members of Governing Board and to Dr. B. R. Raitikar, Principal of Lala Lajpat Rai College of Commerce & Economics for giving me this opportunity to associate myself with the paying of homage to the great memory of Lala Lajpat Rai – one of the noblest sons of India. I deem it a privilege for being able to be here this morning to make my humble contribution. No nation can forget its history and its great men who created history and laid the foundation of a sound socio economic base by their deeds, dedication and profession. Present is a result to some extent of the past, and hence, we owe a great deal to all the great men like Lala Lajpat Rai, Mahatma Gandhi, Lokmanya Tilak, Jawaharlal Nehru and others of the like who by their rare examples of selfless sacrifice, actions, dedicated exertions in the service of the country, and philosophy inspired the people and, continue to do so. Lalaji was a great leader. He was an ardent and devout nationalist. He emphasised self-reliance and self-help to achieve political emancipation. His life is a great example of indomitable courage, self-confidence, tolerance, strong will power, vision, magnanimity, patriotism, compassion and selfless sacrifice. We should all consider ourselves fortunate to have had a leader like him at the crucial stage in our freedom struggle and socio economic reforms.

2

As you all know, he came from a humble but learned family. Lala Lajpat Rai, one of the architects of modern India, was born on January 28, 1865 in a poor Agarwal Bania family in the small village Dhudike in Jagraon Tehsil of Ludhiana District in Punjab. His father was a village school master. His father was a great scholar and was master of three languages: Arabic, Persian and Urdu. His mother had died earlier. He was a good Urdu writer and free thinker. The impact of father and mother on Lalaji was tremendous. His various achievements are well known. However, I think, in order to illustrate his versatility, a few may be recounted. He, along with his other friends, started Dayanand Anglo-Vedic College. He took active part in national movement. The trio of Lal, Bal, Pal (Lala Lajpat Rai, Lokmanya Balgangadhar Tilak and Shri Bipin Chandra pal) became a by-word in Indian Politics, as representing the spear-head of the Indian revolutionary movement. Lala Lajpat Rai took keen interest in the development of social, educational, commercial, cultural and literary activities. Lalaji was very active in the setting up of Punjab National Bank and was its director for some time as he sincerely believed that without a bank of their own, no meaningful progress in the economic and commercial areas could be possible.

3.

Lala Lajpat Rai was truly a national hero. His courage of conviction, nationalistic feelings and his faith in the power of people had earned him the nick name of 'Lion of Punjab'. He was a faithful follower of Gandhiji, Father of the Nation. Talking about Mahatma Gandhi, he once observed : "where in the world shall we find another man equal in spirit or self sacrifice and righteousness to Mahatma Gandhi ? We may or may not agree with his views. We may or may not follow him. But I challenge the whole world to produce another man like Mahatma Gandhi".

4.

It was in Lahore on the afternoon of 30th Oct. 1928 that Lala Lajpat Rai led a mammoth crowd to protest against the Royal Simon Commission. Without any provocation, the British Police Officer started giving lathi blows upon Lalaji's chest. Despite this, he addressed a public meeting against the advice of the doctor who was attending on him. He said, "every blow hurled at us today, will prove a nail in the coffin of British Empire".

Lalaji died on 17th November 1928 as a result of the lathi blows that had been inflicted upon his chest by the British Police Officer, eighteen days earlier, on 30th October; he died a martyr. His life was glorious. His death was equally glorious.

5.

Mahatma Gandhi wrote on his death in "Young India": "Lala Lajpat Rai is dead, Long Live Lalaji. Men like Lalaji cannot die so long as the sun shines in the Indian sky. Lalaji means an institution. From his youth he made of his country's service a religion. And his patriotism was no creed. He loved his country because he loved the World. His nationalism was international. Hence, his hold on Europe and America. They loved him because they knew him. He has bequeathed to younger generation the task vindicating India's freedom and honour. Will they prove worthy of the trust he reposed in them ? Shall we the older survivors, men and women deserve to have had Lalaji as a countryman by making fresh, united, supreme effort to realise the dream of a long line of patriots – in which Lalaji was so distinguished a member ? "

6.

We all will agree that Lalaji has left a precious legacy to us as nation builder, educationalist, writer, orator, trade unionist, journalist and a valiant patriot. Let his memory inspire us to rally round the national tricolour in the present critical hour in history of our Republic.

7.

The president and the members of Governing Board of the college deserve congratulations for their thoughtful action in instituting the Annual Memorial Lecture Series. Such occasions, among other things, do help to remind us of our duties and responsibilities towards the nation and community. They also remind us of the great message of Gita : "To action alone hast thou a right and never at all to its fruits; let not the fruits of action be thy motive; neither let there be in thee any attachment to inaction". In my view, the appropriate way to pay homage to the memory of great leader – Lalaji – is to take a pledge to follow the path shown by him for promoting and preserving the well being of the people.

II

8.

Writing in "Economic Philosophy", Joan Robinson says, "one reason why modern life is so uncomfortable is that we have grown self-conscious about things that used to be taken for granted. Formerly people believed what they believed because they thought it was true, or because it was what all right-thinking people thought". I think, probably, some introspection is needed to set things in proper perspective.

9.

I have chosen to speak on some aspects of capital market in India, particularly, recent trends in this area. There is no particular reason for choosing this topic. However, if I may say so, inspiration for doing so has partly been derived from the strong nationalistic feelings which Lalaji had and which I think, all of us ought to have. This has relevance for economists, too. To quote, Joan Robinson again; "The very nature of economics is rooted in nationalism. As a pure subject it is too difficult to be a rewarding object of study; the beauty of mathematics and the satisfaction of discoveries in the natural sciences are denied to the practitioners of this scrappy, uncertain, ill-disciplined subject. It would never have been developed except in the hope of throwing light upon question of policy. But policy means nothing unless there is an authority to carry it out, and authorities are national. The subject by its very nature operates in national terms .... The aspirations of the developing countries are more for national self respect than just for bread to eat".

10.

As we have noticed in the words of Gandhiji, Lala Lajpat Rai's nationalism was international in connotation. Capital market of any country in the context of the present world has the same universal linkages. "Who can now ask where his country will be in a few decades without asking where the world will be" ? – Lester Pearson, in his R port (1969): partners in Development. Developments, particularly in the financial sector which have occurred in the world in last decade, or so–have been of momentous and far reaching nature. They have tended to bring the world community and their economies much closer than any time in the past. The World no doubt, has become closely interdependent in several respects. Still, there are several aspects of economic management in different countries of the world which make the linkage tenuous in nature. The problem of world issues including debts, for instance, ineluctably leads to the problem of world management. "Debts are not the kind of bond that can unite the world" : observed Herbert Feis in 'Europe, the world's Banker' in 1930. Again this is what the Brandt Report has to say; "The poor will not make progress in a world economy characterised by uncertainty, disorder and low rates of growth; it is equally true that the rich cannot prosper without progress by the poor. The world requires a new system of economic relationships that acknowledge these mutual needs and human interests." This presupposes co-operation between nations. The Brandt Report observes: 'Change is inevitable. The question is whether the world community will take deliberate and decisive steps to bring it about, or whether change will be forced upon us all through an unfolding of events over which the international community has little control,.

11.

It is my view that national economies have to be managed and strengthened with their own skill, resources and expertise to a considerable extent while deriving such inspiration and assistance as are available from outside and striving to achieve the needed cooperation among nations. In the 19th Century, the Western bankers and investors were interested not only in lending but in investing, helping to build railways, steel mills or factories in developing countries like the U.S.A. and Russia, the investment could pay dividends while building up these countries' productive strength. But now the bankers throughout the world are, except in a few cases, to be seen interested in lending than investing. Central banks can create money but not capital. The latter depends upon savings and investments. The role of capital market is to act as an intermediary to collect community's savings and to channelise the same into appropriate productive activities consistent with national priorties. The capital market has thus a crucial role to play in the process of economic development. The intermediation of capital market tends to reduce transaction costs and thus establishes a kind of relationship between savers and investors which facilitates transfer of saving from surplus sectors to the deficit sectors requiring these resources for investment.

12.

The size of capital market is basically determined by the volume and pattern of saving in the domestic economy. For the sake of argument, let us divide the economy into four sectors: Government, Corporate, Household and the rest of World. The Government sector can comprise Government administration and enterprises; similarly, the household sector may be sub divided into non–corporate farm enterprises, non–corporate non–farm enterprises and the household sector proper. The data on saving available for our country, indicate that Government and corporate sectors invest more than that of their own savings and thus are deficit requiring the savings of other sectors for financing their investment activities. Their deficits have to be financed by the household sector and foreign sector. Household sector is the surplus sector and thus its surplus is available to finance the deficits of other sectors. Household sector saves both in the form of financial and physical assets. It is only the former which can be lent to other sector. Thus, it is not the total saving of the household sector but the saving in the form of financial assets which is availble for financing the investment activities of the deficit sectors e. g. Government and Corporate.

13.

It may be of interest to note that with the rapid growth of bank branches, particularly since 1969–the land mark in Indian banking–when the major commercial banks were nationalised–there has been tremendous growth in banking habits. The number of bank branches has gone up from 8262 (end of June 1969) to nearly 42000 branches, including those of Regional Rural Banks now. Total deposits with commercial banks have gone up from Rs.4,646 in June 1969 to nearly Rs. 59,719 crore now. Major portion of these deposits is from the household sector. The Government of India and Reserve Bank of India have evolved policy guidelines under which these saving mobilised by banks are utilised to finance the reqirements of Government through investment in government and semi-government securities – loans and advances to private and public sector industrial borrowers, traders and others. This is known as household sectors' **Indirect** financing of the requirements of deficit sectors. It is indirect because the saving is routed through the intermediation of banks. The revealed preference of the household sector for keeping their saving in the form of deposit with banks is based mainly on the fact that these are safe, liquid, convenient and yield attractive rates of return. Besides, a relationship of trust has been growing between the savers and banks. The transaction cost is also lower than that in the case of comparable lending to the private sector. Besides, lending to the private sector directly makes the saving relatively illiquid.

4.

Household sector also saves in the form of deposits with Post Office, Saving certificates, units of Unit Trust, provident fund contributions, life insurance fund, loans to companies, deposits with non-banking companies and shares and securities. In recent years, because of an improved environment of economic performance, including price stability, the returns on several financial assets in real terms have become attractive and these have tended to strengthen the savers, preferences for financial assets. Total saving of the household sector in the form of financial assets for instance, has increased from 5.5 per cent of net national product (at market prices) in 1970–71 to nearly 10.7 per cent in 1982–83. Of the total savings in these assets, saving in the form of deposits with banks formed nearly 42.4 per cent in 1982–83 as against 38.1 per cent in 1970–71. The proportions of savings in the form of provident fund contributions and life insurance fund have tended to decline, whereas those of loans to companies (including deposits) have improvd their shares. In fact, in 1981-82 deposits with companies increased substantially (by Rs-1304 crores), the increase for 1982-83 is still impressive at Rs. 3608 crores; the outstanding at Rs. 9100 crores forms nearly 15 per cent of the outstanding amount of deposits with banks. Savings in the form of shares and securities of corporate (private financial and non-financial) and co-operative sectors have been very sluggish, the amount in 1970-71 was Rs. 65 crores (out of households' total financial saving of Rs. 2085 crores) this increased to Rs. 180.4 crores in 1980-81 (out of total of Rs. 11,221.7 crores). It was only in 1981-82 that the saving in this form jumped up in an impressive way--to Rs. 366 crores (out of total saving at Rs. 12, 719 crores) --forming about 3 per cent of total saving of the household sector in financial assets--same proportion as it was in 1970-71; the tentative estimate puts it at Rs. 299 crores for 1982-83 (out of total saving of Rs. 15570 crores) The reports are that in the current year also saving in the form of shares and securities of the corporate sector-in particular-debentures--both--convertible and non-convertible-has risen. This in my mind, is a welcome development and let us hope that the confidence which the savers have reposed in the corporate sector will endure.

15.

In recent years, several initiatives have been taken by the autho rities-Government of India and Reserve Bank of India to bring about a diversification in the availability of range of financial assets both by improving the yield and the institutional infrastructural facilities. Integration of the capital markets requires improvement in the rate of indirect financial saving of the household sector. Even in the developed countries like U. S. A. and Japan, the experience shows that this is how the development took place. In the United States, for instance, major part of household sector's saving is in the form of financial assets (deposits and claims on social security institutions) in Japan, nearly 50 per cent of the household sector's saving and more than 80 per cent of its financial saving are in the form of deposits. The development of banking facilities, as already mentioned, augurs well for the promotion of this form of saving in India. Not only this, the allocation policies adopted by the Government of India and Reserve Bank of India are such as to ensure regular and adequate flow of these deposits with banks to the desired and productive sectors of the economy. Unlike in other countries, banks in our country today are financing Agriculture, Industry, infrastructural facilities and trade according to the national priorities of growth with a measure of social justice. Flow of bank credit to hitherto neglected sectors in the economy is being increased through deliberate policies. This is economic necessity.

16.

Banks are giving only working capital funds which is of course, their prime responsibility, but also long term loans to industrial borrowers-small, medium and large. It should be noted that even finance for working capital does enable the borrowers to use their own resources for fixed investment; hence, indirectly the banks finance fixed investment also in this manner.

17.

Historically, the well established enterprises in our country have had somewhat easy access to the banking facilities; they were able to generate internal resources for investment, too. The requirements of new enterprises had thus to be met through other sources-specialised term lending institutions, Government and Reserve Bank of India. I do not wish to elaborate at length this aspect of the development as it is fairly well known by now. The roles of specialised financial institutions in promoting a stable and wide-based diversified industrial structure are praiseworthy; (total loans sanctioned by all the financial institutions amounted to Rs.2826 crores and disbursement to Rs.2060 crores in 1981-82-the increase in sanction over 1980-81 being Rs.601 crores and in disbursement, Rs. 457 crores). In 1982-83 sanctions increased to Rs. 3278 crores and disbursments to Rs. 2367 crores. In addition, increase in commercial banks' loans to medium and large industrial borrowers was Rs. 1230 crores in 1982 (June) over 1981(June)and Rs. 2205 crores (in June 1983 over June 1982). The outstanding amount was only Rs. 1857 crores (Marach 1968) it increased to Rs. 13,418 crores (June 1983)The increase in loans to small scale industries for the same period being Rs 503 crores and Rs. 654 crores, respectively. The outstanding amount which was Rs. 211 crores (March 1968)rose to Rs. 4563 crores (June 1983). Total outstanding loans by commercial banks to industrial borrowers-small, medium and large, stood at Rs. 17,981 crores(end of June 1983)as against Rs. 2068 crores (end of March 1968). In 1983(June) the share of loans to industry had come down to 51 per cent in the total bank credit as against 68 per cent in 1968 (March). However, within this, the share of loans to small industries has nearly doubled during this period. Reserve Bank has not only taken active steps to help set up several financial institutions to cater to the needs of industrial sector, advise and guide them but has also assisted them in their development efforts. For instance, long term assistance given by Reserve Bank itself to specialised financial institutions has gone up from Rs. 30 crores 1971 to Rs. 1, 520 crores in 1982. These figures are being cited to illustrate the flow of credit to the industrial borrowers under the deliberate policies adopted by the authorites. As a Central Bank of the country, it is not only 'Central' but also a'bank' to these institutions. It should be noted that Reserve Bank is not merely a 'lender of the last resort' but also a regular source of funds for assisting developmental activities and institution building. Such examples are rare, in my opinion.

18.

*In recent years, several innovations and practices have been introd*uced by the authorities to allow at least those of the corporate borrowers who have a proven track record of good management and sound financial position to approach the savers directly rather than relying all the time on banks and term lending institutions for the requirements of their fund to some extent. Financial innovation is often viewed as a by product of regulation. The argument is based on the premise that most financial innovations try to circumvent regulatory constraints. No conclusive proof of this hypothesis is available. However, the possibilities of this happening in certain circumstances cannot altogether be ruled out. In India, however, deliberate policy decisions from time to time have been taken by Government of India and Reserve Bank of India to improve the attractiveness of several financial assets for the savers. The result has been that innovations and practices have tended to enhance the ability to bear risk, thereby enabling the savers to invest in shares and securities, among others. The market forces, let us be clear, do help to produce a kind of balance between supply of fund and demand for the same. However, it is debatable whether the same forces enable one to distribute the available fund in the most desired and efficient manner. Distribution is some thing which in my view, requires some regulatory devices.

19.

New sources and uses of fund are innovated when exogenous changes in the environment stimulate the search for new policy tools. Development of futures market and other instruments that facilitates the shifting of portfolio risk have occurred in recent years throughout the world as a reaction to inflationary conditions and volatility of interest rates, increased tax burden and price rise expectations. It has been observed that technology and legislative initiative do tend to respond to economic incentives. I may add that technology which improves physical output and thereby standard of living of the people is as important as financial nnovations which widen and strengthen the financial sector thereby improving general welfare. The recent activities of the capital market in India (as well as abroad) is a reflection of this emerging awareness and recognition; the developments which have occurred as a result of several initiatives taken by the Government and Reserve Bank of India are indicative of this factor.

20.

The buoyant condition of our capital market of the last two-three years is really encouraging and reassuring. It has demonstrated that given proper policy responses, desirable economic incentives, satisfactory performance of the corporate sector, savers' willingness to invest in the shares of corporate sectors can be strengthened. Equity shares, no doubt have failed to evoke the same degree of enthusiasm as has been the case in respect of debentures - convertible - initially, and - non - convertible - now. The precise reasons for this relatively poor response for equity need to be explored in depth. During 1982-83 (April-March), nearly Rs. 705. 30 crores have been raised by way of equity and preference shares and debentures-an increase of 33. 2 per cent over Rs. 529. 36 crores of 1981-82, debentures accounted for 63. 3 per cent in 1882--83 as against 52. 6 per cent in 1981-82. It is worth noting that despite initial revealed preference of savers for convertible debentures in 1982-83, the share of non-convertible debentures in the total rose to 36. 5 per cent from 22.6 per cent in 1981-82. The spectacular response to these issues indicates the extent to which potential saving of the community can be mobilised through appropriate innovations and practices.

21.

It will not be out of place to mention that besides raising the rate of interest and provision of premium on redemption allowed since 1982, the Government adopted further measures to make non-convertible debentures attractive. With a view to providing liquidity to investment in non-convertible debentures, based on the recommendation of the Working Group on "Secondary Market for Debentures" appointed by Reserve Bank of India, companies issuing such debentures have been allowed to have a buy- back arrangement. Under this scheme, companies can buy back non-convertible debentures at par from any debenture where nolding does not exceed Rs. 40, 000 and who has held the debentures for a period of at least one year. Companies in turn can place these debentures with General Insurance Corporation, Life Insurance Corporation and Unit Trust of India, the participating institutions in the scheme. The institutions would purchase these debentures at a discount of $2\frac{1}{2}$ per cent which could be levied as a commitment charge. The withdrawal of the restriction on public financial institutions to subscribe or underwrite debenture issues of FERA/MRTP companies has also helped such issues. The financial institutions have been permitted to underwrite/subscribe, amongst themselves, upto 50 per cent of any debenture issue made by FERA/MRTP companies. Similarly, the procedures have been further simplified relating to the investment by non--residents of Indian nationalty/origin (including overseas companies, partnership firms, societies and other corporate bodies owned to the extent of 60 per cent by non-residents of Indian nationality/origin as well as overseas trusts in which at least 60 per cent of the beneficial interest is irrevocably held by such persons) and repatriation of such proceeds and investments. All these measures have been taken to widen the role of capital market.

22.

It is hoped that these measures will continue to prove attractive enough to the savers thereby enabling the corporate sector to raise the needed resources for investment. It has been noticed that well established companies or new companies set up by well known names/managements, have been relatively more successful than brand new companies in raising capital through these devices. It is not altogether unexpected. It is hoped that companies raising resources through these devices will continue to improve their performances and management images to keep the capital market in a continued state of healthy condition. It is essential if the bubble is not to burst.

23.

It is one way to raise capital. It is quite different to utilise the same efficiently. In our system, domestic saving has increased from 12.1 per cent of net national product (1970-71) to 16.8 per cent (1982-83); the corporate sector saved only 0.6 per cent - of net national product, the same as in 1970-71. It is necessary, therefore, that the corporate sector improves its saving performance. Besides, as is widely reported, capital - output ratio is relatively high in our country. To some extent, let us admit, it is inevitable because of the strategy of development adopted in which pointed priority is given to certain highly capital intensive and long gestation types of activities - oil exploration, petrochemical, fertiliser, irrigation, power generation, etc. However, capital is ought to be used efficiently and productively and therefore, every effort will need to be made to improve operational efficiency to get the maximum out of every rupee mobilised and invested. This is a managerial challenge and it has to be faced if the savers' willingness to save in the form of shares and debentures is not to be diminished.

24.

I may also mention that there is a gap in the financial system at present. That relates to the raising of capital by new entrepreneurs - unknown names. They will, no doubt, continue to be helped by the specialised financial institutions, including banks in their efforts. Still, some thought needs to be given to set up a kind of risk or venture capital fund to assist new entrepreneurs, in particular, those who wish to adopt high and modern technology. As we are aware, in our technical laboratories, there exist several innovative devices but have not been put to commercial exploit ation - may be for lack of adequate support - financial or otherwise. Risk capital foundation of Industrial Finance Corporation, in my view, is helping those who have already demonstrated that they can put the existing/available technology for commercial exploitation successfully; this does not, however, support experimentation with the existing/new technology from the beg-ining to the stage of commercial exploitation. This needs to be given some attention particularly, at this stage of our development - may be in areas of electronics.

25.

Venture capital funds, specialising in risky investment in new firms, have sprung up from America to Western Europe, Japan, South Korea and Singapore. Stock markets where new firms can float their shares have come up in the past three years in London, Paris, Amsterdam, Stockholm Munich and Tokyo. The status of people who succeed in business on their own is on the rise in Europe and much of Asia including India. The victorian moralist, Samuel Smiles, once observed; "The spirit of self help is the root of all genuine growth in individual; and, exhibited in the lives of many; it constitutes the true source of national vigour". This spirit--latent and otherwise--needs to be encouraged by all innovations and practices, particularly because of quickening pace of technical change, failure of old industries and the growth of new industries. It may be relevant to note what Prof. John kenneth Galbraith has to say in this respect:

"It is a common impression, not discouraged by scientists, engineers, industrialists, that modern scientific, engineering and industrial achi-evements are the work of a new and quite remarkable breed of men. This is pure vanity".

26.

Entrepreneurs are not inventors. They are the people who, given the right and timely assistance, can short circuit the otherwise long time lag within established firms between having a new idea and doing some-thing about it. They are prone to grab opportunities, others are slow to exploit it. Modern industry relies heavily on brain power--not on brawn. Hence, the necessity to constantly innovate and search for new ideas and ways of doing things better, quicker and more efficiently. It has been said that most successful venture capitalists learn about business by working for industrial companies, observing the methods and practices of those in the management of these successful ventures--not by working for banks or securities houses. Management of investment portfolio is entirely different from growing companies. Resources are to be mobilised; this is important. However, more important than this is to use the same efficiently, productively and in conformity with national priorities and objectives.

III

27.

The most significant of the recent activity on Indian capital market has been the tremendous capacity of investors to absorb increasingly large issues of securities of private corporate sector. Though the new issues market is but only one segment of the capital market, it is not isolated from the rest of them and as such the phenomenal rise in new issues activity reflects the vigour of the Indian capital market. The other important component of the Indian capital market, namely the public financial institutions, has also recorded considerable rise in their operations over the years. Besides these, there have been some policy initiatives which have long term implications for the development of capital market. Moreover, the Indian capital market has also to adjust to the challenges thrown by its own growing size and diversification. In the present environment when even the international financial market is undergoing a crisis, it would be of general interest to discuss the issues before the capital market and the future prospects.

28.

The term capital market refers to facilities and institutional arrangements for the borrowing and lending of long term finance. In the broad sense, capital market may be said to consist of a series of channels through which the savings of the community are made available for investment in the industrial and commercial enterprises. The Indian capital market which comprises the unorganised sector, mainly the indigenous bankers and the moneylenders and the organised sector, consisting of bank ing system, stock market, specialised institutions and insurance corporations, now presents a well-integrated structure to meet the varied needs for capital of industrial, agricultural and trading sectors of the economy.

29.

It needs to be noted that the evolution of Indian capital market as it obtained since Independence has been through various policy measures deliberately designed to widen and strengthen it, so as to quicken the tempo of institutionalisation of saving and investment needed for economic progress. The two broad segments of the organised sector of a capital market are (i) industrial promotion, developmental and financial institutions, and (ii) the stock market. While the stock market in India has started much before the country gained independence, the set-up of institutional infrastructure for promotion of industries is a post-independence development.

30.

The Government of India, consistent with its policy of playing an active role in the economic development of the country, took appropriate steps towards creating a net-work of financial institutions. Accordingly, the Industrial Finance Corporation of India (IFCI) was set up in 1948; State Financial Corporations (SFCs) were set up from 1951 onwards. The Industrial Credit and Investment Corporation of India (ICICI) was set up, with the support of Indian and foreign financial institutions and banks, under the Companies Act, 1956. The Reserve Bank of India has not only been playing the role of traditional central bank but also of promoting appropriate financial infrastructure. The promotional role of Reserve Bank has been noteworthy. The Refinance Corporation for Industry Ltd. (RCI) was set up in 1958 by the Reserve Bank to enable banks to extend medium and long term finance to industries, while the Government of India set up in 1955 the National Small Industries Corporation to extend promotional and financial assistance to small scale industrial sector.

31.

The Industrial Development Bank of India (IDBI) was set up in 1964 by Reserve Bank of India as the apex institution for providing term finance to industries and for coordinating the activities and operations of other institutions in the field of industrial finance. IDBI had been assigned a definite developmental role in the area of industrialisation. IDBI also took over the business of RCI. It was followed during the same year by the creation by RBI of Unit Trust of India (UTI), with a view to mobilsing the savings of the communtiy and investing in corporate securities in such a way as to secure safety, liquidity and ensure regular and growing returns to the unit holders. This was the arrangement by which savers could invest indirectly in the shares and securities of private corporate sector. The institutional set up at regional level was further strengthened by the establishment of State Industrial Development Corporations (SIDCs) and State Industial and Investment Coporations (SIICs). In the background of the growing problem of industrial sickness, a new corporation namely the Industrial Reconstruction Corporation of India Ltd. (IRCI) was set up in 1971 with the sole objective of providing rehabilitation and reconstruction assistance to sick and closed industrial units or those facing imminent closure. Thus, the institutional framework for taking care of the industry-from 'cradle to the grave' was developed.

32.

The nationalisation of life insurance business, major scheduled commercial banks and general insurance brought into the State's fold a wide net-work of institutional set up to meet the varied demands for capital of the growing industrial sector.

33.

These institutions which can be classified (i) on the basis of their organisation into statutory bodies (IDBI, IFCI, SFCs, UTI, LIC, etc.) and companies (ICICI, IRCI), (ii) by their functions into industrial promotional and development banks (IDBI, IFCI, ICICI, SFCs, SIDCs/SIICs) and investment institutions (LIC, UTI, GIC, banks) and (iii) by their area of operation into all-India institutions (IDBI, IFCI, IRCI, UTI, LIC, GIC, ICICI) and state level institutions (SFCs and SIDCs/SIICs) present the whole gamut of institutional infrastructure for industrial finance in the country.

34.

Unlike the establishment of financial institutions which came into being after Independence with the initiative of Government of India and

Reserve Bank of India, the institution of stock market is fairly old. However, regulation of stock exchanges on an all-India basis was attempted only in the mid-fifties when the Securities Contracts (Regulation) Act, 1956 was enacted, though efforts were being made in this direction from the beginning of the post-war period. In the State of Bombay, there was a framework of legislation in respect of future transactions in shares; otherwise the growth of stock exchanges was totally unchecked. In the boom, conditions, stock exchanges used to spring up at many places, at times more than one within a city, and vanish once the boom was over.

35.

The Securities Contracts (Regulation) Act, 1956 provides for a general system and apparatus of control to ensure fair dealing and to protect investors, without detailed or meticulous regulatory provisions relating to any specific matter. The Act permits only those stock exchanges to function which are recognised by the Central Government. The recognised stock exchanges may, subject to the previous approval of the Central Government, make rules and bye-laws for the regulation and control of contracts.

36.

At present, there are twelve recognised stock exchanges in the country. These are at Bombay, Ahmedabad, Calcutta, Madras, Delhi, Hyderabad, Bangalore, Cochin, Indore, Kanpur, Pune and Ludhiana. A few more are expected to come up soon. The establishment of stock exchanges at different centres provides greater facilities for transactions to the investors spread all over the country and also enable the companies to raise funds. The stock market plays a vital role in facilitating the performance of the two important aspects of a capital market, namely the raising of new capital in the form of shares and debentures and the trading in securities already issued by companies, thereby providing a measure of liquidity to the shares.

37.

New issues market in the country is regulated through the Capital Issues Control Act. New capital issues can be classified into three types (i) issues requiring prior consent of the Controller of Capital Issues (CCI), Government of India, which include Issues to be made at a premium, all issues by MRTP companies, debenture issues to be offered to the public for amounts exceeding Rs. 50 lakhs in a period of one year, bonus issues and issues of preference shares and debentures carrying participation or conversion rights; (ii) issues requiring acknowledgement of the CCI i.e. issues of securities, other than those stated above by public limited companies for amounts exceeding Rs. 50 lakhs in a period of 12 months; and (iii) exempted issues, mainly the issues of non-MRTP companies for amounts less than Rs. 50 lakhs.

38.

The Central Government has from time to time taken steps to encourage new issue activity. The recent steps in this direction include the guidelines for issues of debentures by public limited companies to meet their modernisation/expansion cost or to augment their long term capital. In a series of measures starting with guidelines for issues of rights debentures in 1978, the Government of India has tried to make investment in debentures attractive in terms of yield, maturity and liquidity.

39.

Simultaneously, with the encouragement to companies to mobilise larger funds from the market, Government has instituted a variety of measures to widen the ownership pattern of shares. The most important of these measures is the guidelines for listing of shares on stock exchange-the guidelines require that the public offer of share be greater than a specified minimum percentage of issued capital.

40

Another measure of encouraging wider distribution of share ownership is the prescribed procedure for the allotment of shares when a public issue is oversubscribed. In the present rules, the allotment is in favour of small applications. The Government has also allowed various tax concessions to encourage investment in shares. Dividends earned from companies, alongwith income from other specified assets upto a total of Rs. 7,000 per year, are exempted from income tax. Investors are allowed a deduction from their total income of an amount equal to 50 per cent of the amount invested in equity shares of a new industrial undertaking upto maximum investment of Rs.20,000. As a measure to widening distribution of share ownership by tapping the market outside the metropolitan centres and to serve the investors from different parts of the country, new stock exchanges at some more places have been granted recognition.

41

Government has also liberalised the facilities for investment in Indian

dian companies by the non-residents of Indian nationality or origin and overseas companies, firms, societies, trusts and other corporate bodies predominantly owned by such non-residents.

42.

Direct investment without repatriation facilities in the new issues of Indian companies engaged in any business activity, except real estate business, are allowed upto 100 per cent of the issued capital. However, direct investments on repatriation basis are permitted upto 40 per cent in new issues of shares and convertible debentures of any new or existing company (other than FERA company) raising capital through a public issue with prospectus for setting up new industrial/manufacturing projects or for expansion/diversification of existing industrial manufacturing activities. But under a scheme for encouraging the non-resident Indians to in*vest in priority industries in India, investment* in *shares and convertible* debentures upto 74 per cent is permitted.

43

Limited facilities for portfolio investment by the non-resident Indians in shares/debentures of companies through stock exchanges have also been introduced. Investment in shares and each series of convertible debentures of any one company not exceeding one per cent of the paid up value by single investor with an aggregate ceiling of five per cent is being allowed without permission. Investment in excess of five per cent requires prior permission of the Reserve Bank.

44.

As a measure to encourage *investments by the non-resident In*dians, Government has granted certain tax concessions. The incomes out of these investments as well as long term capital gains arising on transfer of such investments are taxed at flat rate of 20 per cent plus surcharge. Beside, such investments are also exempt from wealth tax; gifts of these assets made by Indian citizens and persons of Indian origin settled abroad to their relatives in India are also exempt from gift-tax.

45.

All these measures reflect the innovations and incentives provided by the Government of India to widen the choice of financial instruments to investors, thereby widening and strengthening the role of capital market.

IV

46.

The organised sector of the Indian capital market largely caters to the long term capital requirements of the corporate sector. The origin of corporate sector in India dates back to the middle of 19th century, when the Companies Act, 1860 gave it a legal status and the 1857 Act introduced the principle of limited liabilities in Company Law. At present, the corporate sector operates under the Companies Act, 1956.

47.

There has been a vast growth in the number of companies in the country during the last two decades. The number of non-government companies more than doubled (from 26,007 in 1961 to 70,795 as at the end of March 1982). The number of non-Government public limited companies during the same period increased from 6,702 to 9,530. Simultaneously, the number of companies listed on stock exchanges increased from 1,203 in 1961 to 2265 in 1980. The paid-up capital of listed companies increased from Rs. 675 crores to Rs. 3,212 crores, indicating a rise of 154 per cent in the average paid up capital per listed company. Before analysing the impact and magnitude of institutional assistance in financing corporate sector, it may be useful to refer briefly to the growth and pattern of overall savings of the economy.

48.

There has been an increase in net domestic savings which at current prices increased from Rs. 542 crores in 1950-51 to Rs. 24,678 crores in 1981-82. The marginal income-saving ratio consistently increased, from slightly less than 17 per cent in the Third Plan period (1961-66) to nearly 36 per cent in the Fifth Plan (1974-79) and further to over 39 per cent in 1981-82. It may be mentioned that the share of savings in financial assets in the total domestic savings increased from 3.5 per cent in 1950-51 to 52.5 per cent in 1981-82, and the ratio of financial assets to income increased from less than one-half per cent in 1950-51 to 9.7 per cent in 1981-82 reflecting an impressive growth in financial assets which was made possible by the rapid growth of financial institutions, banking facilities as well as the emergence of a well differentiated institutional structure of the capital market.

49.

The data of annual average level of investment in the corporate sector indicate a rise of over fifty-times in this respect during Sixth Plan (1980-85) from that of during the first Plan (1951-56). The average annual investment increased from Rs. 80 crores in the first Plan period to Rs. 4 427 crores in the First three years of Sixth Plan. At the same time, data on sources of finance indicate an increasing reliance of corporate sector on the external funds. The corporate savings (i. e. retained profits) which financed 44.1 per cent of corporate investment during the First Plan, contributed only 15.7 per cent during the first three years of the Sixth Plan (Table-1).

50.

During the last decade, the term lending institutions operating at the national and regional levels have emerged as a significant source of term finance to industry. Most of these institutions have had come into being before the Sixties, but the aggregate assistance of these institutions, though by itself sizeable, was not higher than the capital directly mobilised by companies on the market. But the picture changed drastically during the seventies. The corporate sector came to rely on the institutional funds for investment. The aggregate institutional sanctions (i. e. by the IDBI, IFCI, ICICI, IRCI. LIC, UTI, SFCs, SIDCs) increased almost twelve-fold from Rs. 254 crores in 1970--71 to Rs. 3191 crores in 1982-83. Similarly, disbursements of assistance by these instituions increased sharply from Rs. 160 crores in 1970-71 to Rs. 2355 crores in 1982-83 (Table-2).

51.

Capital raised by companies through issues of shares and debentures, after remaining almost stagnant at around Rs. 100 crores a year during the sixties and upto late seventies has shown a sudden spurt during the last few years. The available data relate to capital raised by non-government companies against consent/acknowledgement of their proposals by the Controller of Capital Issues (Table – 3) To that extent the data are partial, but nevertheless reflect quantum of funds directly mobilised by the corporate sector on the market.

52.

Capital raised by the corporate sector has shown a tremendous rise in the last few years. A striking feature of the capital raised is that a substantial portion of it is through debentures-the equity capital has also increased-though not to the same extent. The rise in capital raised through debentures came largely on account of certain favourable policy changes in the guidelines for debenture issues. As mentioned earlier, a Working Group under Shri N. N. Pai, the then *Chairman* of IDBI, was appointed by RBI (1981) fo considering the issues relating to the development *of a secondary market* for debentures. *Based on the recommendations*, Government of India have revised the guidelines for issue of debentures. Efforts have been made to develop primary as well as secondary markets. The maturity as well as the rate of return on these debentures have been made attractive. Non-convertible debentures of seven years maturity now carry an interest rate of 15 per cent and companies have discretion to redeem them at premium of 5 per cent. For enhancing the liquidity of investment in debentures, a buy-back scheme with a participation of financial institutions has been introduced whereby small debenture holders (upto Rs. 40,000) can after holding for a minimum period of one-year sell back the debentures to the company which in turn, can place them with the participating financial institutions (viz. LIC, UTI and GIC) at a discount of 2.5 per cent which can be levied as commitment charge. The rate of interest on convertible debenture is 13.5 per cent per year. In order to make non-convertible debentures attractive enough, companies are permitted to pay a premium upto 5 per cent of the face value at the time of redemption. The Government also revised upward ranging between 0.25 and 1.50 percentage points in underwriting commission, brokerage and managing broker's commission in respect of public issue of capital; this was to encourage underwriters and brokers to put in more efforts to popularise the instrument among investors.

53.

The spurt in equity capital, on the other hand, is reflective of the expanding corporate sector and also the increasing interest of investors in equity shares. The dilution of foreign shareholding by FERA companies also contributed to a great extent to investors' interest in equity shares.

54.

Public response to capital issues has been selective and has been better to equity issues and debentures (which normally can be issued by an existing company) of existing well-established companies. Issues by new companies, however, had to rely on support of financial institutions. This is understandable.

55.

The enlarged activity in the primary market gave buoyancy to the secondary market and the major stock exchanges of the country experienced substantial boom during the last few years, barring occasional spells of bearishness. An idea about the buoyancy in the stock market can be had from the fact that the RBI's all-India index number of ordinary share prices (average annual) recorded rise of 21.4 per cent in 1978-79, 9. 8 per cent in 1979-80, 11. 5 per cent in 1980-81 and 20 per cent in 1981-82. The index, however, was down by 5. 7 per cent in 1982-83. However, the stock market was not without ups and downs, and the working of leading stock exchanges was often disrupted by payment crisis arising out of excessive speculation and by unscheduled closures. Government issued directives from time to time to regulate their working and has also broadbased the governing board of the Bombay Stock Exchange by providing for nomination of three public representatives and a representative of the Reserve Bank. With a view to ensuring orderly management of Stock Exchanges, the Government issued certain directives in January 1983 to all Stock Exehanges. Accordingly, the time for performance of hand delivery contracts in active scrips traded on the Bombay, Calcutta, Delhi, Madras and Ahmedabad stock exchanges has been extended to three months from 14 days. Moreover, the stock exchange authorities are required to (a) have the accounts of active members audited every year by qualified Chartered Accountants and forward a copy each of these accounts to Stock Exchange Division of Ministry of Finance; (b) amend suitably their by-laws to extend suitable regulatory measures to non-cleared securities so that speculative activities in such securities are brought under control; and (c) inspect periodically the books of accounts of at least 10 per cent of active members a year and institute necessary disciplinary action against members whose books of accounts reveal malpractices like excessive trading, under-reporting of transactions, trading in securities prior to listing, etc. and submit to Stock Exchange Division of Ministry of Finance, Government of India, a quarterly report giving full details of such inspections and the disciplinary action taken.

56.

It needs to be recognised that the working practices of stock Exchanges have crucial impact on the mood of the market. It is not only what the Stock Exchange does but also what is generally believed and seen what it is doing is important for influencing the investors' psychology. The management of the Stock Exchanges has to be efficient and impartial enough to impart and retain the needed degree of confidence of the investors. In India, there is nothing like Securities Exchange commission to scrutinize and oversee the functions of the Stock Exchanges. Hence the need to be ever vigilant is greater. Stock Exchanges are the windows of capital market and ears in a way-through which investor operates. In India, the investing public is not yet fully sophisticated, the level of understanding of the various aspects of the functioning of corporate setor is somewhat insufficient. The educative role which the Stock Exchange has to play in winning and retaining confidence of investors is of high order and crucial importance.

57

According to a RBI Study, in terms of the value of shareholding, individuals held 37.6 per cent of the paid-up value of sample companies, joint-stock companies held 33.8 per cent and the public financial institutions 25.7 per cent. The study relates to ownership patteru as at the end of 1978, but brings out the role of public financial institutions in supporting the primary market for corporate securities. The analysis of shareholding in the new companies revealed that the financial institutions contributed as much as 42.6 per cent of paid up capital compared with 32.1 per cent by individuals and 22.6 per cent by joint stock companies. The corporate sector's increasing dependence on institutions is further reflected in the fact that an earlier survey (in 1965) had shown the share of financial institutions to be less than 25 per cent. The dominant role played by all-India promotional and developmental institutions, viz. IDBI, IFCI and ICICI as also by the State level institutions in promoting joint-sector companies is quite evident from this.

58.

It may be of interest to refer to certain relevant factors of corporate sector financing. In this connection, a reference may be made to the studies conducted by the RBI on company finances based on the balance sheets of a sample of about 400 large Public Limited companies (i. e. those with paid up capital of at least Rs. 1 crore) and a sample of over 1200 Medium Public Ltd. Companies (i. e. those with a paid-up capital of more than Rs. 5 lakhs and upto Rs. 1 crore). The period covered is 1971-72 to 1977-78 (Table 4).

59.

It will be observed from the Table 4 that these companies show a heavy dependence on internal generation of funds and long term borrowings, partly from institutions and partly in the form of deposits. The contribution of the capital market in financing asset formation is very small, barely 5 per cent, even for the large companies which may be expected to have relatively good access to the capital market. The contribution of debentures is negligible, amounting to less than 1 per cent of the increase in gross financing. Deposits constituted the biggest external source of medium funds. Internal funds provided more than three quarters of the gross financing and non-market long term borrowing contributed around a fifth.

60.

New issues of shares (also debentures) can be made through a rights issue to share holders or to the public by prospectus. Of the amount issued by prospectus, about a third is usually allotted prior to the public offer to directors,shareholders, institutions and government, the balance is offered to the public. There has generally been over-subscription of a large proportion of issues by existing companies and a smaller proportion of issues by new companies and substantial under subscription of some issues. The important reason for relatively small amounts of capital being raised from the public in the form of equity is the thinness of trading in the shares of existing companies. Shares of private limited companies are not eligible for listing on the Stock Exchanges and their stocks are not traded in the market. Listing on the Stock Exchange is important for a company's shares to be easily traded. The dominant shareholders and the financial institutions together are commonly stated to hold often 80 per cent of the outstanding share capital of existing companies. Consequently, the floating stock available for trading in the market tends to be limited. The dividend yield on ordinary shares is generally much low in relation to the return on deposts. The main attraction of ordinary shares is the potential for capital gains. If the companies based on their performance do not have a good track record, the average investor develops an aversion and cautious approach towards equity shares.

61

Preference shareholders enjoy preferential treatement over equity holders in their dividend income which is fixed. The preference shares are generally cumulative i. e. if a company skips its preference dividend for a particular year/s, it cumulates each year and becomes payable when the company is able to pay; the preference shareholders have a preference over the equity shareholders in repayment of capital in case of company's dissolution or liquidation. Preference shares cannot exceed one-third of total paid-up capital and reserves. The ceiling on dividend is 13.50 per cent as fixed by the Controller of Capital Issues. Although preference shares do not benefit from high earnings as ordinary shares, they are less risky for the investor compared with latter. From the company's point of view, preference dividends offer no tax advantage as they are paid from after tax profit. Thus, they are substantially more expensive than debentures and may be used only to get around the debt-equity ceilings.

62.

The debenture holder is a creditor of the company and is not treated as owner like shareholders. The debentures are of four categories viz. registered, secured and unsecured, redeemable and convertible. Debentures in general are redeemable either at the issue price or at a higher price and can be reissued by the company. The most popular form of debentures is the convertible ones which can be converted into ordinary shares of the issuing company under specified terms and and conditions. The investors prefer convertible debentures because of right for equity shares, anticipation of increased dividends, higher opportunity benefits due to realisation of appreciation earlier than to wait till maturity and income-tax exemption on dividends upto a certain limit.

63.

From the point of view of a borrowing company, debentures are a very attractive means of raising long term funds. Raising debenture capital does not dilute control, unlike shares and borrowing from term lending institutions with a mandatory convertibility clause. Unlike ordinary and preference shares, the servicing of debentures is tax deductible, reducing the after-tax cost by half. This is the characteristic that debentures share with other forms of borrowing, except that 15 per cent of the interest paid on deposits is not deductible. However, this source of finance is gaining popularity with the raising of ceiling on rate of interest to 13.50 per cent on convertible debentures from March 1981 and to 15.00 per cent on non-convertible debentures from April 17, 1982.

64.

Deposits raised from public are unsecured and involve a non-negligible risk of default even by large companies. Acceptance of deposits by non-financial companies is regulated by the Department of Company Affairs. Certain categories of deposits are completely excluded from the *purview of regulations (the exempted categories include deposits from* shareholders of private limited companies, directors of public limited companies, Governments and specified financing institutions, etc.) *Excluding* the exempted categories, the regulations prescribe ceilings for the quantum of deposits that can be accepted by companies in relation to their paid up share capital and free reserves (net worth). Regulation of the acceptance of deposits by non-financial companies is necessary to protect the interests of depositors. A desirable strategy would be to encourage the growth of alternative debt instruments (such as debentures) that would prove more attractive both to companies and to depositors. The acceptance of deposits from the public for periods more than 3 years has been prohibited with effect from April 1, 1978 in terms of 'Companies (Acceptance of deposits) Rules, 1975'. The Public Sector Companies pay maximum 14 per cent interest on 3 years' deposits and well-established Private sector Companies pay upto 15 per cent interest on 3 years, deposits accepted by them from the public. According to available data, the growth rate of company deposits shot up from 18.9 per cent in 1978 to 31 per cent in 1980; the rate of growth in 1983 has been 66 per cent. The increase in such deposits was Rs. 3609 croresın 1983 over 1982, (March). as against Rs 1304 crores in 1982 over 1981. This indicates the growing popularity of deposits with non-banking companies.

V

65.

The Indian capital market is now fairly developed and through a chain of institutional agencies and stock exchanges, it is well equipped to mobilise the savings of the community and channel it into productive investments.

66.

It is, however, obvious that the Indian capital market still continues to be mainly supported by the public financial institutions. The corporate sector's recent efforts to mobilise funds directly on the market also had the institutional underwriting support & were considerably facilited by feworable changes, Particularly in the guidelines for debenture issues. Thus, the major problems before the Indian Capital market are directly or indirectly related to the reasons at the command of the public financial institutions & the performans of the corporate Sector the institutional underwriting support and were considerably facilitated by favourable changes particularly, in the guidelines for debenture issues. Thus, the major problems before the Indian capital market are directly or indircetly related to the resources at the command of the public financial institutions and the performance of the corporate sector.

67.

At the time when the developmental institutions themselves are facing resource constraints, a judicious allocation of their funds is necessary so that the pace of industrialisation is not hampered. It is, therefore, necessary that the existing companies, which on their own can mobilise funds directly meet increasing portion of their financing requirements from outside the financial institutions. The institutions may in that event be able to meet the requirements of new companies.

68.

Since 1971, all-India term lending institutions (viz. IDBI, IFCI, ICICI, LIC and UTI) are required under the guidelines issued by Government of India to introduce a convertibility option on all loans of more than Rs. 50 lakhs. This limit has since been raised to Rs.1 crore* and the institutions have been directed not to acquire more than 40 per cent of the share capital through conversion, except in special circumstances where they can go up to 51 per cent with the approval of the Government. The convertibility clause was introduced as suggested by the Industrial Licensing Policy Inquiry Committee with two-fold objectives; to share in the prosperity of assisted companies and to facilitate stronger participation in the management of assisted companies, where required, to meet social objectives. This provision has evoked resentment from companies.

69.

As mentioned already, assistance from term lending institutions - in the form of loans, underwriting, subscription to securities - has increased over years. In view of the increasing incidence of industrial sickness and the problem of restraints being faced by term lending institutions, it is necessary that these institutions whose stakes in borrowing companies are increasing, are provided with adequate powers not only to safeguard *their investments* but also to ensure proper and *efficiant* use of the funds.

* Subsequntly in giudelines have been revised. The limit hase been further rai ed to Rs. 5 crores with effect from 1. 3. 84 and financial institutions have been advised not to stipulate under normal circumstances the convertibility clause where the combined equity holdings by all the allIndia financial institution (including the investment institutions) exceed 26 per cent in the case of non MRTP companies and 40 per cent in the case of MRTP companies/Large Houses.

70.

For an active primary market for securities, a healthy and well-functioning secondary market is necessary. In the context of Indian capital market, this has become all the more crucial that stock market works smoothly and in imaginative and dynamic fashion. Not only the number of securities being traded on the stock market and the number of investors have increased, but also the recent relaxations regarding portfolio investments by non-resident Indian and overseas bodies predominently owned by them have given an international dimension to our stock market. An effective regulation of stock exchanges operation and the necessary reforms in their practices have become imperative to avoid excessive speculation leading to frequent disruption of their functioning. The Securities Contracts (Regulation) Act was enacted in 1956 and since then there have been certain basic changes in the working of stock market, the most important being the banning of forward trading in 1969. But in the absence of effective control, the ban remained on papers only and speculation continued. The existing regulatory mechanism appear to have proved ineffective in tackling the emergent problems on stock market. It is, therefore, felt that the securities Contracts (Regulation) Act is reviewed and an agency on the lines of Securities Exehange Commission of the USA is established in the country to oversee the working of stock market on a regular basis. The functioning of stock market should be such as to inspire and retain the confidence of investing public.

71.

I may also draw your attention to the other problem i. e. the problem of 'take-over' of management. Ever since the advent of joint-stock company, the concept of the 'take-over' has existed and we are aware that in the past, the managements of companies have changed hands through the transfer of stocks. Apriori, the transfer of controlling interest on mutually negotiated terms and conditions does not appear objectionable, like the transfer of any other asset, but in the context of industrial securities such transfers may have repercussions on others, particularly, the minority shareholders. With a view to safeguarding the interest of minority shareholders, the stock markets of western countries like the UK, USA have devised certain norms whereby in the case of any bid for takeover, all shareholders are offered the same terms and conditions. However, in our country such a system is yet to come into being, mainly because till recently the takeover bids were rare or if any, affected only a small segment of investors class. But with the increasing instituitutional holding of corporate stocks and the flow of funds of non-resident Indian investors, together with increasing awareness amongst the investing public, the issue of take over requires attentiion. I think, appropriate guidelines may have to be thought of in this behalf to preserve and promote a healthy tradition.

72.

This in brief represents the changing face of Indian capital market. The size and features of the capital market have thus evolved alongwith the strategies adopted for industrial and agricultural growth which besides, sound economic reasoning, have been guided by the social objectives of balanced regional development, creation of employment opportunities and an equitable distribution of gains of growth. A noteworthy feature of the growth of Indian capital market is that over the years the organised sector of the market has been so enlarged and strengthened through a wide network of institutional infrastructure that the area of the unorganised sector is gradually shrinking. The capital market is increasingly getting integrated through several initiatives taken by the Government of India and Reserve Bank of India. The market is also being exposed to ideas, technology and a measure of competition.

73.

At the same time, establishment of term lending institutions in the public sector, the nationalisation of life and general insurance business, and major scheduled commercial banks have helped the authorities to introduce measures leading to increasing institutionalisation of saving and investment. This also enables the authorities to ensure proper allocation of savings of the community among different users - Government, corporate and household sectors.

74

Given the socio-economic objectives of the growth adopted, such a regulated flow of funds is desirable. The policy framework has been flexible enough; it has responded to the changing needs of the economy. With the increasing pace of industrialisation, the successive Industrial Policy Statements have allowed a greater scope for private sector.

75.

The trends in capital raised by companies indicate their increasing resort to debentures. This is a healthy development. This device, however, will benefit the established companies with a good track record. The new companies may not be able to mobilise resources through this instrument. To the extent resources are raised through capital market directly by companies, their dependence on lending institutions (and banks) for loans should be expected to diminish. The term lending institutions and banks will then be able to provide support to new industrial ventures and other desirable activities. The gradual shift in savings preference of household sector from physical assets to financial assets, the spread of banking network throughout the country, the increasing equity-cult and the entry of non-resident Indians' saving into corporate securities have considerably broad based the Indian capital market. The Indian capital market, therefore, appears to be well poised to meet the increasing requirements of the corporate sector.

76.

I may add that mobilising resources is an important task. However, more important than that is adequate steps to use the same efficiently and productively. It is only when the resources mobilised get utilised efficiently that the investing public and the community can derive benefit on an increasing basis.

77.

I would like to end by aptly quoting Lala Lajpat Rai who while talking about wealth and power said, "In any struggle between nations, the victory eventually must rest with the one in possession of the largest number of 'Silver bullets'. It is true that silver bullets alone will not do unless there are brains and bodies to use them, but the latter without the former are helpless".

Table 1 : Corporate Sector – Savings and Investments

(Amount in crores of Rupees)

	First Plan (1950–51 to 1955–56)	Second Plan (1956–61)	Third Plan (1961–66)	1966–67 to 1968–69	Fourth Plan (1969–70 to 1973–74)	Fifth Plan (1974–75 to 1978–79)	Sixth Plan (1979–80 to 1981–82)
	1.	2.	3.	4.	5.	6.	7.
Investments	404 (80.80)	1,374 (274.80)	2,663 (532.60)	1,432 (477.33)	4,041 (1347.00)	10,226 (3408.67)	13,281 (4427.00)
Savings	178 (35.60)	398 (79.20)	634 (126.80)	231 (77.00)	1,205 (401.67)	1,708 (569.33)	2,088 (696.00)
Savings as percentage of investments	44.1	28.8	25.8	16.1	29.8	16.7	15.7

Note : Figures in brackets are annual average for the plan period.

Source : Compiled from various issues of Report on Currency and Finance — Reserve Bank of India.

Table - 2 : Assistance sanctioned and disbursed by Financial Institutions *

(Amount in crores of Rupees)

Years	Loans		Underwr ting		Total	
	Sanctions	Disbursements	Sanctions	Disbursements	Sanctions	Disbursements
1.	2.	3.	4.	5.	6(2+4)	7. (3+5)
1970-71	214.4	138.7	39.8	21.2	254.2	159.9
1976-77	908.2	553.9	68.6	43.4	976.8	597.3
1982-83 (Provisional)	2980.2	2202 3	210.4	152.7	3190.6	2355.0

* Include IDBI, IFCI, ICICI, IRCI, LIC, UTI, SFCS, SIDCs

Source : Report on Development Banking in India, IDBI and data for 1982-83, received form respective institutions.

Table - 3 Capital raised by non-Government public limited companies (against consents/acknowledgements)

(Amount in crores of Rupees)

Year	Equity shares	Preference shares	Debentures	Total
1961	56.8	5.4	11.8	74.0
1971	35.2	6.2	8.7	50.1
1981	157.2	–	130.5	287.7
1982	113.9	2.5	277.9	394.3

Source : Controller of Capital Issues, Government of India.

Table 4 : Sources and uses of funds of large and medium size public limited companies 1971 – 78

(All figures represent annual averages of flows for the whole period)

	Large companies		Medium companies	
	(Rupees crores)	Percentage of gross total assets	(Rupees crores)	Percentage of gross total assets
Net fixed assets	211	37	43	41
Net working capital [1]	79	14	– 1	– 1
Depreciation	282	49	62	59
	573	100	104	100
Depreciation	282	49	62	59
Other internal funds [2]	181	32	18	17
Capital issues	26	5	5	5
(Shares)	(22)	(4)	(5)	(5)
(Debentures)	(4)	(1)	(–)	(–)
Others long term borrowing	94	16	22	21
(Deposits)	(52)	(9)	(9)	(9)
(Banks)	(5)	(1)	(4)	(4)
(Institutions)	(5)	(1)	(4)	(4)
(Governments)	(22)	(4)	(–)	(–)
(Others)	(11)	(2)	(4)	(4)
Others (net)	– 11	– 2	– 2	– 2
Total financing	573	100	104	100

1. Current assets minus current liabilities.
2. Paid-up capital, reserves other than depreciation, surplus and non-current provisions.

Source : Department of Statistical Analysis and Computer Services, Reserve Bank of India : Special tabulations.