External Commercial Borrowings (ECBs)

- ECBs refer to the commercial loans in the form of bank loans and other debt instruments like bonds from the overseas lenders with a minimum average maturity of 3 years.
- Reasons behind its popularity is the lower interest rate on the loan and increase in foreign exchange inflows.
- All Corporate Entities, SEZs, NGOs in Micro Finance and Low Cost Housing Projects are allowed to borrow under ECBs in India.
- RBI regulates the ECB market in India.

Foreign Currency Convertible Bonds (FCCBs)

- Is an International Debt Instrument like ECB
- These bonds are issued by an Indian company to the foreign investors to raise funds from abroad and are expressed in foreign currency
- These bonds can later be converted into ordinary shares of the company.

Depository Receipts (DRs)

- Using it an Indian Company can deposit shares with a domestic bank which instructs a foreign depository to issue DRs to foreign investors

- **American Depository Receipts(ADRs)** are DRs listed on U.S Stock Exchange while **Global Depository Receipts(GDRs)** are normally listed on European Stock Exchanges.

- ADR/GDR, on one hand, allows Indian company to raise more funds and also allows foreigners to invest in Indian companies without inconvenience of cross-country or cross-currency transactions.

- **Indian Depository Receipt(IDR)** is a DR created by an Indian Depository (NSDL or CDSL), against the underlying shares of foreign companies.

- On SEBI approval IDRs can be listed on Indian Stock Markets.

- **Derivatives**: It is a financial instrument whose value depends on the value of some other underlying asset like shares, commodities etc.

- **Futures Contract:** A derivative instrument in the form of an agreement to buy or sell an asset in specified quantity, on a specified date at a specified price.

Financial Futures: Refers to futures with shares as the underlying asset.

Example:

- **Options:** It is a contract that gives the right but not an obligation to buy or sell the underlying asset of a futures contract

- Options less risky than futures.
- **Futures & Forwards:** Similar contracts except that Futures are Formal market instruments traded in share market or other organized market while Forwards are informal market instruments (Over the Counter trading).

- **Call option** gives the holder **right to buy** an underlying asset while **Put option** gives **right to sell.**

- **Commodity Futures/Derivatives:**
  Derivatives where underlying asset is a commodity like agricultural products, metals and natural resources.
- It allows one to gain from Speculation while another entity can hedge. e. g. Agricultural derivatives allow farmers to hedge.

- Commodity Derivatives traded at **Commodity Exchanges**- National Commodity & Derivative Exchange(**NCDEX**) & Multi Commodity Exchange (**MCX**) being the most important ones, both operating since 2003.

- **Forwards Market Commission (FMC)** is the regulator of the market.

- **Currency Futures**: It is a contract to buy or sell one currency against another in specified quantity on a specified date & price & is traded on a stock exchange.

- This market allows the exporters & importers to hedge against the ER volatility.

- RBI and SEBI jointly regulate this market.

- **Participatory Notes (P Notes):** Financial derivative used by the investors like Hedge Funds abroad to invest indirectly in the Indian share market as these are not registered with SEBI unlike the FIIs.

- Hedge Funds are risk taking investment companies which make huge profits but not registered with SEBI.

- **Mutual Funds**: Funds operated by an asset management company (AMC) which raises money from public and invests it in a group of assets like shares and bonds.

- Net Asset Value (NAV) of a MF is the value of all assets held by MF minus the expenses on managing funds divided by the number of units issued.
- Return from a MF depends on change in NAV over time.

Classification of MFs:

- **Equity Funds & Debt Funds**: MFs investing only in shares are called Equity Funds (e.g. Index Funds) while those investing only in debt instruments like bonds are called Debt Funds (e.g. Gilt Funds).

- **Balanced Funds**: Mutual Funds which invest both in equity and debt instruments. Equity investment is to increase return. Debt investment is to reduce risk.

- **Open & Closed Ended Funds:**
- Funds in which both entry & exit of investors are open are called open ended funds. These funds can grow dynamically as any one can bring in their investment any time
- In closed ended funds, investment can only be made during limited period called New Fund Offer(NFO) &after it both entry & exit is closed
- However, the units of closed ended funds can be traded in secondary market.
- NAV of closed ended fund tends to be higher than an open ended fund of similar size

- **Exchange Traded Funds:**
  - ETFs track the value of some underlying asset & are like substitute for direct investment in that asset.
  - For example, Gold ETFs track the gold prices and their value will fluctuate with gold prices. It is substitute for direct investment in gold & were encouraged recently when India faced higher CAD due to higher imports.
  - ETFs are traded in share markets & despite being mutual fund are similar to shares

- **Central PSE (CPSE) ETFs**
- A unit of CPSE ETF represents a weighted average of share value of 10 PSUs.
- Attractive to investors as are less risky that separate investment in share market.
- Government used CPSE ETFs as a tool for disinvestment
- All ETFs are different from traditional Mutual Funds as portfolio of underlying asset can not be changed in ETFs.