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Financial Markets

Overview

In April 2008, except for the equity markets, all other segments of the financial markets have been subdued as they responded to the macroeconomic fundamentals. Even though the Indian equity markets have been buoyant, they have been the third worst performer among the emerging markets as the domestic concerns relating to surging inflation and indications of slowdown began to gather momentum. The fourth quarter results of 2007-08 have been mixed with some sectors such as consumer durables; telecom and IT have performing well but other sectors not displaying good results. Overall, it appears that the growth in sales and net profits have been lower than in the corresponding quarter a year ago as there have been larger increases in expenditures on both raw materials and compensation to employees in selected companies. But the biggest concern has been due to the rapidly rising inflation rate, which has been consistently ruling above 7 per cent and the authorities have been forced to undertake a number of fiscal and supply-augmenting measures, given the supply constraints as well as global factors driving up the inflation rate. The Finance Minister has expressed concerns about the rising inflation and accepted sacrificing growth in order to contain the rise in prices. Even the Prime Minister has called an unscheduled meeting of his cabinet to discuss the measures necessary to combat the surging inflation, though he finally cautioned against knee-jerk reactions.

The significant monetary measures have been taken by the RBI, to manage inflationary expectations. It has unexpectedly, on April 17, announced an increase in cash reserve ratio (CRR) by 50 basis points from 7.5 per cent to 8.0 per cent in two tranches of 25 basis points, each effective from April 26 and May 10, thereby impounding a total amount of Rs 18,500 crore. Further, in the annual policy statement on April 29, the RBI has held the base rates steady but increased the CRR by yet another 25 basis points to 8.25 per cent with effect from the fortnight beginning May 24; the market sentiments became buoyant.

With the looming inflationary concerns, there has been a sharp decline in the commodities futures trading, especially among the agricultural commodities. Despite intense opposition to the imposition to the Cash Transaction Tax (CTT) from the two major commodity exchanges as well as from the regulator Forward Market Commission (FMC) due to the possible migration of trading to international exchanges and possible spurt to dabba

trading, the finance minister has preferred to retain the tax; in fact he characterised the regulators as representing the interest of the exchanges and trying to put pressure on the authorities.

Incidentally, the Raghuram Rajan committee on financial sector reforms has made a slew of recommendations by placing importance on inclusion, growth and stability as important objectives in the reform process; however there have mixed reactions pertaining to its applicability in the present milieu.

Trends in the Equity Market

i) Primary Issues

10.1: Primary Issues in the Month of April 2008

Name	Date of Issuance		Offer Price (in Rs)	Issue Size (in Rs cr)
	Opening	Closing		
Aishwarya Telecom Limited	15-Apr-08	17-Apr-08	32-35	14.0
Total				14 (627)

Note: Figure in bracket is for the previous year.

Source: *Various media sources*

During the first month of the current financial year, there have been only one issue mobilising an aggregate amount of Rs 14 crore as against Rs 627 crore raised in the corresponding month last year (Table 10.1)

IPO Price Status

On April 23,2008, Pawan Kumar Bansal, Minister of State for Finance, informed in Parliament that, more than half of the total number of IPOs listed on the bourses in the last two years are trading below their offer price, with one-third trading at a discount of 40-60 per cent. During April 1, 2006-March 31, 2008, the number of IPOs listed on the Bombay Stock Exchange (BSE) stood at 150, of which 86 are trading below their offer price; of these, 36 IPOs were trading at a discount of more than 40-60 per cent of the issue price. On the National Stock Exchange (NSE), of the 162 IPOs listed during the same period, 88 were trading below the issue price and 38 at a discount of more than 40 per cent of the issue price.

Table 10.2: Resources Raised through Public and Rights Issues

	April-Mar 2008		April-Mar 2007	
	No	Amount (Rs crore)	No	Amount (Rs crore)
Public Isues	92	54,511	85	29,797
IPOs	85	42,595	77	28,504
FPOs	7	11,916	8	1,293
Rights Issues	32	32,518	39	3,711
QIP	36	25,525	25	4,963
Preferential Allotment*	398	61,589	302	17,183
Total	558	1,74,143	451	55,654

Source: SEBI Bulletin, April 2008

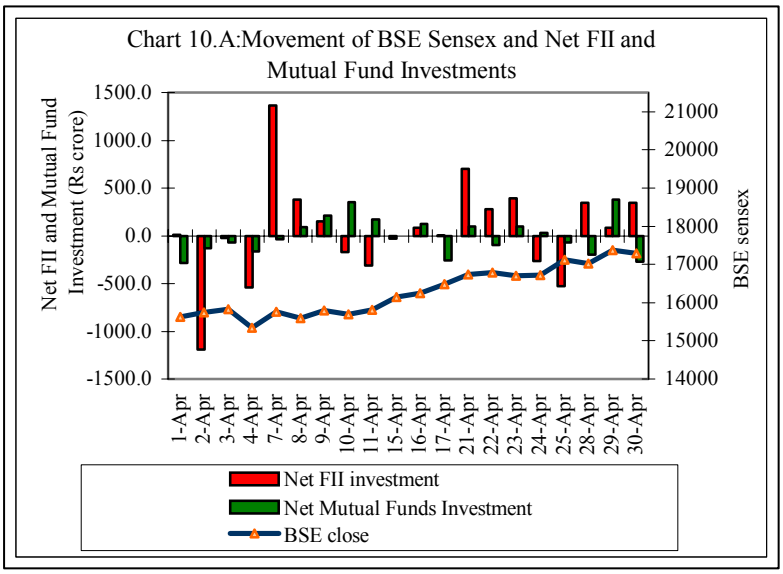
During April-March 2008, Rs 1,74,143 crore have been raised from the primary market through 558 issues compared with Rs 55,654 crore rasied through 451 issues in the

same period during the corresponding period of the previous year. During April-March 2008, 398 preferential allotments raised Rs 61,589 crore as compared to 302 issues that raised RS 17,183 crore during the period April-Mar 2007 (Table 10.2).

Delisting Guidelines

After a wait of almost two years, the government and the Securities and Exchange Board of India (SEBI) have firmed up their views on finalising the guidelines for delisting of companies from stock exchanges. Despite differences of opinion, the reverse book-building process remains the choice for finalising the delisting price of shares. In its draft proposal, SEBI has mooted a fixed price for delisting, which will be a 25 per cent premium over a fixed floor price. The fixed floor price is to be calculated by an accredited rating agency. SEBI has mooted the alternative price discovery method as it considers that the reverse book-building process has failed to serve its purpose of fixing fair exit value for shareholders, giving disproportionate powers to public shareholders for cartelisation in price discovery. Meanwhile, the issue of a threshold level of shareholding to be decided on delisting still remains a cause of disagreement. In its presentation to the finance ministry, SEBI has given two options. Promoters should either acquire at least half of the public shareholding in their respective companies or buy shares that will take their shareholding to a little over 90 per cent, whichever ensures a larger number of shares.

ii) Secondary Market



The month began with a subdued market sentiments due to change in tax treatment of securities transaction tax (STT) as well as the concerns about potential losses of corporates on forex derivatives resurfaced after the Institute of Chartered Accountants of India (ICAI) asked companies to disclose losses on a marked-to-market basis incurred on derivatives trades from the current financial year onwards (year ending March 2008), as a precursor to making a new accounting standard (AS-30) mandatory from 1 April 2011. As the early corporate results displayed buoyancy, the

indices surged further. Even the 50 basis points hike in CRR has had marginal impact on the market sentiments. Given the buoyancy in global markets, the domestic markets also turned buoyant and the BSE Sensex has touched the 17,000 mark and then even closed above the benchmark at 17,287 as the market sentiments have been positive as RBI choose to held the rates steady while effecting a 25 basis points hike in the CRR. Despite volatile FII and mutual funds investments, BSE Sensex has continued to surge as shown in Chart 10.A.

Given the buoyancy in the market sentiments, the total turnover on NSE has risen to Rs 2,71,227 crore in April from Rs 2,53,012 crore in March and the market capitalisation has also increased to Rs 54,42,780 crore from Rs 48,58,122 crore. Similarly, the total turnover on BSE has risen to Rs 1,15,446 crore as against Rs 1,10,875 crore in March. However, the daily average turnover has dipped to Rs 5,772 crore from Rs 6,166 crore. The P/E ratio for the BSE Sensex 30 scrips has fallen from 25.53 in January to 20.71 in April.

Sales Practises

SEBI has suggested a series of measures for brokers (trading members of the exchange), in a discussion paper on the issue of sales practices to be followed by them in a kind of do's and don'ts format, in an attempt to fulfill its twin objective of investor protection and the interests of the capital market. The discussion paper wants the main broker to be responsible for the wrong deeds of one of his constituents –the sub broker, or the franchisee. SEBI wants brokers to give their clients an exposure limit that is commensurate with the financial details that the clients report in the KYC document. SEBI has also introduced the concept of 'introducer' prevailing in the banking sector.

These proposals have fetched qualified responses in terms of spirit and reservations against certain details. The broking and analyst community feels that SEBI needs to define some of the concepts and in some places mention specific quantitative numbers or change the emphasis. According to Mr Vijay Murmuria, President of Association of National Stock Exchanges Members of India (ANMI), the concepts such as "excessive trading" and "risk appetite" need to be defined and marked out clearly in terms of numbers, lest an element of subjectivity should creep in and create confusion. Mr Arun Kejriwal, an independent analyst, agreed that conceptually risk profiling or understanding risk appetite or having a benchmark for excessive trading are good, but these required quantifications in terms of numbers in relation to an individual and also market time.

Financial Standing

The ANMI President felt that the emphasis on "financial standing" for an introducer of a retail investor was misplaced. "When client's PAN Card, I-T return/proof residence are insisted upon, the financial standing of the introducer is uncalled for, as he is not being asked to stand as a guarantor. Mention of an introducer's social or professional standing (with some recognisable identification) may be in order," the ANMI chief felt. The head of equity division of an large brokerage with national presence and with substantial retail clientele felt that getting an introducer ready to declare his/her financial standing might be very difficult, if not altogether impossible. Mr Kejriwal was of the opinion that why an individual would like to dilute his/her right to privacy for introducing an investor. "This proposition is not realistic as no introducer is likely to come forward as the cost of this personal declaration. On the contrary, there could emerge a breed of introducers, who would do this job for a payment." Regarding retail investor's networth, the ANMI president felt, the proposed guidelines need to be re-looked. Accepting the SEBI suggestion that clients might be required to have certain minimum amount of networth (e.g Rs 5 lakh) for trading in the derivative segment, ANMI appears to have doubts whether a client's balance sheet would reveal his or her true networth all the time. The ANMI President said: "We are studying the SEBI proposal and would soon send in our appropriate response to the regulator." Mr Kejriwal felt that for derivatives trading a system of mandatory certification could be introduced to avoid mis-selling such products. He also felt that it was worth revisiting definition of an analyst and a journalist recommending buy and sale. A few analysts at broking firms felt the SEBI prescribed timeframe for purchase or sale by an analyst should be reviewed in view of fairness, as SEBI said no research analyst might buy or sell any security that he or she follows or derivative of such security, for a period beginning 30 calendar days before and five calendar days after the publication of a research report concerning the stock.

Direct Market Access

SEBI has allowed brokers to offer their institutional clients direct access to the exchange trading system through the brokers' infrastructure, which named as the direct market access (DMA) facility. This allows clients anywhere in the world to access the broker's trading platform without any manual intervention. The DMA facility offers advantages such as direct control of clients over orders, faster execution of client orders, reduced risk of errors associated with manual order entries, greater transparency, increased liquidity, lower impact costs for large orders, better audit trails and better use of hedging and

arbitrage opportunities through the use of decision support tools/algorithms for trading. SEBI has directed the exchanges to prepare a model agreement. Based on risk assessment, credit quality and available margins of the client, the broker will ensure that trading limits/exposure limits/position limits are set for all DMA clients.

Rajan Committee

The committee on financial sector reforms headed by Raghuram Rajan has recommended that provident funds and insurance companies should be allowed to invest abroad, a move that will require legislative changes. The committee has said that the SEBI needs to establish a speedier and new product approval process and introduce new methods of price discovery, clearing and settlement while the central bank should refrain from intervening in the foreign exchange market to modulate the exchange rates. Given the pressure of huge capital flows, the committee suggests that the government should liberalise the financial markets and make them more open to foreign players.

Further the committee has recommended that regulatory actions should be subject to appeal at a Financial Sector Appellate Tribunal, which will be set up along the lines of, and subsume, the existing Securities Appellate Tribunal to ensure that there are more direct checks on the regulator in a system that is less rule-bound. In another suggestion, the committee has said regulatory staff should be given higher remuneration, and should be drawn from the private sector; he further cautions that reasonable precautions need to be put in place to avoid conflicts of interest. In another significant recommendation, the report has said that supervision of all deposit taking institutions must come under the Reserve Bank of India. Accordingly, it has called for the Ministry of Corporate Affairs to review accounts of unlisted companies; SEBI should review accounts of the listed ones.

Margins

On April 17,2008, SEBI has allowed institutional clients in the cash segment of the equity market to maintain their margin in the form of approved securities. These approved securities cover any instrument under the Securities Contract and Regulation Act (SCRA). The market regulator has directed the stock exchanges to issue necessary guidelines to operationalise this. Currently, the retail segment only pays the margin for both the cash and the derivative segments. Institutions only pay margin for the derivative segment. Margin payment by the institutions will be implemented from April 21, 2008. In a major relief, SEBI has permitted them to maintain their entire margin in the form of approved securities. SEBI

had earlier asked institutional investors to deposit margins for trades carried out by them in the cash segment. The SEBI decision comes into effect from April 21. Institutional investors and foreign institutional investors (FIIs) in particular were opposed to the SEBI idea of levying margins on institutional trades in the cash segment. But the regulator's argument was that when it was creating a level playing field by allowing FIIs and institutional investors to short-sell in line with retail shareholders, they should also cough up margins as paid by the retail shareholders. Earlier, SEBI has been expected to allow the deposit of at least 50 per cent of the securities held by institutional investors as margins against the exposure in the cash segment. To prevent misuse of client collateral, SEBI has reiterated the need for brokers to maintain proper records of such collaterals. SEBI has also directed brokers to issue a daily statement of collateral utilisation to the clients.

Short-selling

Short-selling in the equities market, which is to start from April 21, may be a slow starter, with major domestic institutions like insurance companies and banks staying away from it. According to Section 6 of the Banking Regulation Act and the Securities Contract Regulation Act, banks are not allowed to short-sell. It will require an amendment to the Act if banks were to short-sell and RBI is not in favour of this. Even for lending and borrowing of equities to facilitate delivery-based short-selling, banks will require a separate provision from RBI. The Insurance Regulatory and Development Authority (Irda) too is not in favour of insurance companies short-selling equities. Irda is of the view that insurance companies cannot short-sell in the equity market as it amounts to speculation and the Act does not permit speculation with policyholders' money. However, it is in the process of framing guidelines for insurance companies to engage in lending and borrowing of stocks to earn on the idle portfolio.

Listing Agreement

SEBI has made the provisions of Clause 49 of the listing agreement more stringent. If the non-executive chairman is a promoter or is related to promoters or persons occupying management positions at the board level or at one level below the board, at least half of the board should comprise independent directors. Earlier, SEBI had mandated that a third of the board should be independent directors if the chairman was a non-executive one. SEBI has also specified the minimum age of an independent director, at 21. SEBI amended certain provisions in the master circular and made it clear those disclosures of relationships between

directors inter-se both of executive and independent directors will have to be made in specified documents/filings. SEBI also said that the gap between resignation/removal of an independent director and appointment of another independent director in his place should not exceed 180 days.

Sectoral Indices

Among the sectoral indices of BSE, barring capital goods index all other indices have registered positive gains. With the depreciation of the rupee, the IT sector indices have again recorded the highest gains during the month followed by consumer durables index. As the RBI choose to hold the interest rates steady, the bankex and auto sector indices too have closed for the month in a positive zone (Table 10.3).

Table 10.3: Monthly Percentage Change in the Stock Indices of BSE

Index	Base Year	March 2008 Closing	April 2008 Closing	April		Percentage Change for the Month
				High	Low	
SENSEX	1978-79	15644.44	17287.31	17480.74	15297.96	10.50
BSE Mid-Cap	2002-03	6427.82	7138.74	7214.53	6221.45	11.06
BSE Small-Cap	2002-03	7841.62	8773.57	8886.65	7658.38	11.88
BSE 100	1983-84	8232.82	9199.46	9312.29	8062.58	11.74
BSE 200	1989-90	1932.41	2157.52	2183.34	1892.09	11.65
BSE 500	1998-99	6157.27	6885.03	6965.79	6024.18	11.82
BSE TECk	Apr 02,2001	3024.13	3472.49	3528.20	2976.83	14.83
BSE PSU	1998-99	7426.83	8081.53	8140.83	7154.31	8.82
BSE AUTO	Feb 01,1999	4524.77	4726	4739.28	4363.62	4.45
BANKEX	Jan 01,2002	7717.61	8819.68	9068.43	7486.47	14.28
BSE CG	Feb 01,1999	14009.02	13931.25	14231.19	12326.57	-0.56
BSE CD	Feb 01,1999	3883.29	4543.11	4630.45	3799.42	16.99
BSE FMC	Feb 01,1999	2290.07	2461.38	2470.61	2282.50	7.48
BSE HC	Feb 01,1999	3848.11	4275.1	4283.69	3800.39	11.10
BSE IT	Feb 01,1999	3547.61	4261.93	4340.60	3506.63	20.14
BSE METAL	Feb 01,1999	14022.56	16114.4	16318.18	13297.46	14.92
BSE REALTY	2005	7554.8	8505.49	8795.88	7058.95	12.58
BSE OIL&GAS	Feb 01,1999	10016.82	11505.79	11770.54	9965.93	14.86
BSE -POWER	Jan 03,2005	3189.81	3338.81	3378.20	2922.15	4.67
Dollex 30		3215.04	3498.36	3556.60	3131.29	8.81
Dollex 100		2131.87	2345.78	2381.56	2079.46	10.03
Dollar 200		805.32	885.39	898.52	785.91	9.94

Source: BSE (www.bseindia.com)

Similarly, all the S&P Nifty indices have registered gains over the month and again the IT indices have outperformed the broader indices. Even the gains on the small and mid cap indices have exceeded those recorded by the broader indices (Table 10.4).

Table 10.4: Monthly Percentage Change in the Stock Indices of NSE						
Index	Base Year	March 2008 Closing	April 2008 Closing	April		Percentage change for the month
				High	Low	
S&P CNX Nifty	1995	4734.5	5165.9	5230.75	4628.75	9.11
CNX Midcap	2003	6240.7	7004.8	7084.55	6065.90	12.24
CNX Nifty Junior	1996	7975.8	9171.0	9272.25	7699.35	14.99
Nifty Midcap 50	2004	2371.7	2741.2	2763.70	2318.35	15.58
S&P CNX Defty	1995	4105.9	4411.0	4486.80	4013.65	7.43
S&P CNX 500	1994	3825.9	4222.1	4266.00	3738.40	10.36
CNX 100		4537.9	4988.0	5048.65	4435.60	9.92
CNX IT	1996*	3704.95	4357.65	4435.10	3627.25	17.62
BANK Nifty	2000	6655	7629	7815.90	6446.70	14.64
India VIX			25.16	42.49	21.34	

Note:*the base value has been changed from 1000 to 100 with effect from May 24, 2004
Source: NSE (www.nseindia.com)

In a landmark development, the NSE has launched the country's first Volatility Index (VIX) on April 08, 2008. The VIX is a measure of the market's expectation of volatility over the near term (next 30-day period) calculated as annualised volatility denoted in percentage terms and based on the Nifty 50 index option prices. After launching the new index, Ravi Narain, MD and CEO, NSE, said that the Volatility Index is a good indicator of the investors' perception on how volatile markets are expected to be in the near term. The VIX is calculated using the methodology adopted by the Chicago Board of Options Exchange (CBOE), which was the first to introduce volatility index in the US in 1933. The Indian index will derive the implied or expected volatility from the near- and mid-month options bid and offer prices of the Nifty 50 index options. From the options bid and offer prices, an indicator can be derived about the degree of volatility investors expect in the market. This volatility figure, denoted in percentage, would be the India VIX value.

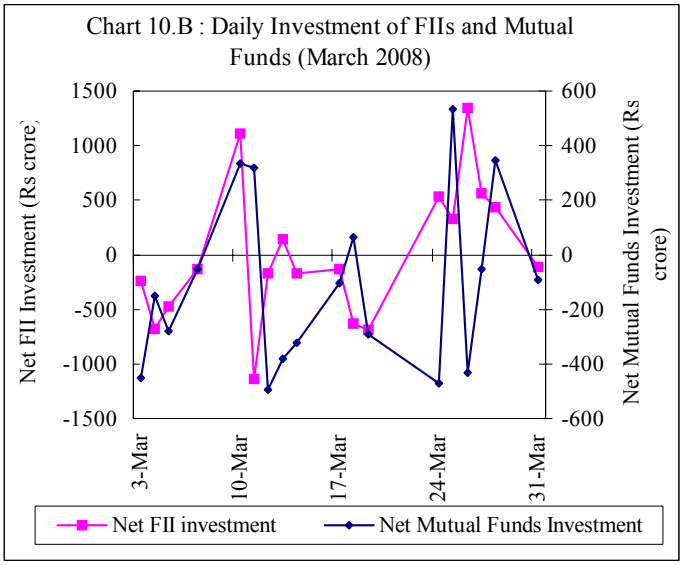
According to Ravi Narain, NSE is considering listing of Nifty futures or Nifty exchange traded funds in the US market. Currently, Nifty futures are traded on Singapore Stock Exchange and Nifty exchange traded funds are listed on London, Frankfurt, and Milan exchanges. Combined assets under management of Nifty ETF listed on London, Frankfurt, and Milan amounts to $400-500 million. NSE has granted licences to three European funds to launch Exchange Traded Funds (ETFs) and was looking to enhance foreign participation

through Indian Depository Receipts (IDRs). The cumulative assets under management of the three funds would be about $400 million.

Foreign Institutional Investors (FIIs) and Mutual Funds

The FIIs have been net buyers of equities in April to the extent of Rs 1,075 crore as compared with Rs 130 crore in February but much lower than that in April 2007 at Rs 6,679 crore. In April 2008, the FIIs have undertaken purchase of Rs 62,516 crore and sales of Rs 61,441 crore. However, the cumulative net investment of FIIs in the first four month oif the calendar year 2008 has been negative at Rs (-) 10,358 crore with purchase of Rs Rs 311,130 crore and sales of Rs 321,488 crore. The number of FIIs registered has increased to 1334 in April as against 1319 in March and the number of sub-accounts has risen to 4019 from 3964 (Chart 10.B).

Mutual funds have continued to be net sellers of equities for two consecutive months. They have net sellers in March to the extent of Rs 1,971 crore and in April, to a smaller extent of Rs 112 crore. In April, they have purchased securities worth Rs 13,407 crore and sales of Rs 13,518 crore.



The month of April has witnessed huge inflows given the buoyancy in equities market. The inflows through existing and new offers have been Rs 517,106 crore while redemptions have been to the extent of Rs 445,626 crore resulting in a net inflow of Rs 34,903 crore. Among the various schemes, the bulk of inflows under existing schemes have been under liquid and money market schemes followed by income schemes. However, under new schemes launched, the income schemes have attracted the bulk of investors' interest. The asset under management (AUM) has increased to Rs 573,411 crore in April as against Rs 538,508 crore in March, a net inflow of Rs 34,903 crore.

Among the different asset management companies, the AUM, in the case of BOB Asset Management Co ltd has increased from Rs 92 crore as on 30th April 2007 to Rs 52,549

crore as on April 30, 2008. Similarly, the AUM under Reliance Capital Asset Managemnet ltd has more than doubled to Rs 99,849 crore as on April 30, 2008 from Rs 48,828 crore in April 2007.

New Fund Offers (NFOs) are making a comeback after a lull in the previous two months, due to a stabilising equity market. This is in contrast to last year when investors were lure d by a flood of NFOs. The fund houses are now rolling out products, which were held over for the last few months owing to weak market sentiments. Confidence of investors as well as fund houses to come up with the new products encouraged by attractive valuations and strengthened liquidity. Sundaram BNP Paribas Mutual Fund recently launched its Financial Opportunities and Entertainment Opportunities Fund, AIG Investments launched world gold fund, and ICICI Prudential launched Focused Equity Fund.

According to a report released by Value Research, mutual funds made a turnaround in April after three months of negative performance. In, all categories of funds, on an average, gave positive returns with the diversified equity gaining 8.36 per cent. The returns have varied between a high of 17.3 per cent and a low of 1.69 per cent. The majorities have returned between 7 per cent and 11 per cent. This was broadly in line with the BSE Sensex that gained 10.5 per cent and the S&P CNX Nifty, which gained 9.2 per cent. The only losers in the last month were gold ETFs, which track the price of gold. These funds lost 6 per cent during the month in line with the performance of the yellow metal in international markets.

According to the latest report by domestic brokerage company Sharekhan, mutual funds are gathering on Rs 23,545 crore of cash, which is waiting to be deployed in the market. Of this, Rs 19,214 crore lies with existing mutual funds, while the remaining Rs 4,331 crore has been mobilised through NFOs. As the market continued with uncertainity, fund managers have decided to play it safe as is quite evident from the cash position (percentage of net assets) of the various funds. According to an analysis of the equity portfolios of March, funds have been in most liquid form. This will not only insulate the fund from abrupt fluctuations as much as possible, but also give the fund managers ample leeway to cherry pick as and when the market throws up great opportunities. Out of the entire mutual funds industry, diversified equity funds were having cash of Rs 7,859 crore (8.64 per cent of the total assets) at the end of March against Rs 4,773 crore (4.46 per cent of total assets) in January 2008. According to them, 108 diversified equity funds increased their cash allocation expressed as percentage of net assets, while 33 saw a decline. The 11.6 per cent fall in the overall fund flow was due to the 31 per cent reduction in the amounts mobilised through

NFOs coupled with a 27 per cent rise in redemption volumes, it stated. In line with the sharp fall in equity markets, all sector funds had generated negative returns in February 2008. Fast moving consumer goods funds gave the highest returns in February 2008, followed by pharmaceutical and automobile funds. Mutual funds have slashed their exposure to banks, power and housing and construction companies and have bought stocks in pharmaceutical, telecom and oil and gas sectors.

REMFs

Paving the way for domestic asset management companies (AMCs) to invest directly in real estate, market regulator SEBI unveiled the much-awaited guidelines for real estate mutual funds (REMFs), which mandated that at least 35 per cent of the corpus of a scheme been invested directly in real estate assets. The remaining funds can be allocated for mortgage-backed securities and instruments of companies in the sector. The investments in real estate assets and real estate-related securities have to be less than 75 per cent of the net assets of the scheme. According to experts, real estate mutual funds (REMF), which have been launched on April 25, 2008, will help the real estate sector to be more organised and transparent while providing retail investors with a new avenue in a relatively stable asset class.

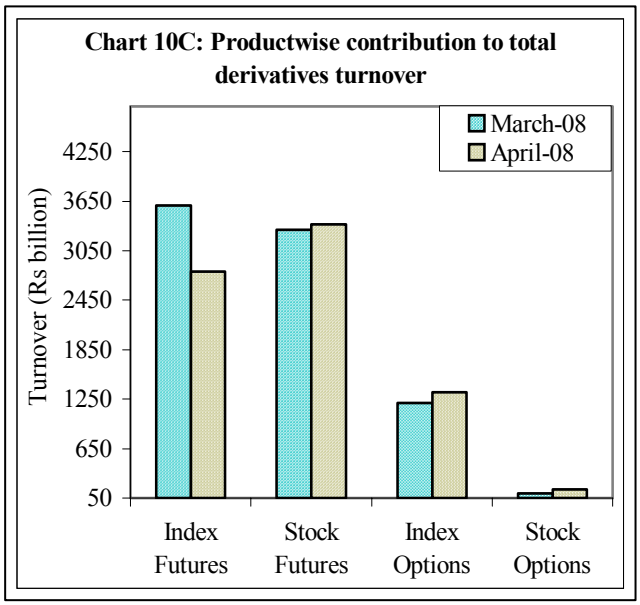
Mutual Funds Overseas Limit

On April 03, 2008, RBI raised the overall limit for overseas investment by domestic mutual funds from $5 billion to $7 billion, with a view to providing greater opportunity for investment overseas.

Private Equity

Private equity (PE) investments in India have grown to $4 billion in the first quarter ended March 31 of calendar year 2008, two times more than the value registered during the corresponding period last year. Through this, India has maintained its position as the hottest investment destination in Asia (excluding Japan) and has even surpassed China, which has recorded just $570 million so far. In 2006, China received $13 billion in PE investments in 2006 compared with India's $7 billion.

iii) Derivatives



There has been a decline in the turnover in the equity derivatives market. The total turnover has declined from Rs 821,215 crore in March to Rs 766,431 crore in April. The daily average turnover has fallen from Rs 45,623 crore to Rs 38,322 crore. However, the percentage of open interest to daily average has risen from 139 per cent in March to 159 per cent in April, implying increased positions being held by the investors. The turnover in index futures has declined from Rs 359,970 crore to Rs 280,100 crore while that of stock futures and index options have marginally increased over the same period (Chart 10.C) (Table 10.5). However, the ratio of derivatives to cash market turnover has declined from 3.3 per cent in March to 2.8 per cent in April.

New Regulations

The Institute of Chartered Accountants of India (ICAI) has asked all companies to disclose and/or provide for all losses on derivative contracts, except for forward contracts, where a company needs to comply with accounting standard AS11.

The announcement on accounting for derivatives issued by ICAI on March 29, 2008, clarifies the best practice treatment to be followed for all derivatives is as follows:

(i) All derivatives except forward contracts covered by AS 11, can be accounted for on the basis of the requirements prescribed in AS 30, Financial Instruments: Recognition and Measurement.

(ii) In case an entity does not follow AS 30, keeping in view the principle of prudence as enunciated in AS 1, 'Disclosure of Accounting Policies', the entity is required to provide for losses in respect of all outstanding derivative contracts at the balance sheet date by marking them to market.

The effect of the above announcement is as follows:

(i) In case an entity does not follow AS 30, the losses in respective of derivative contracts at the balance sheet date have to be provided for and disclosed.

(ii) In case an entity follows AS 30, then the effect will be broadly as follows:

In case the derivatives do not meet the hedge accounting criteria as laid down in AS 30, the gains or losses in respect thereof will have to be recognised in the statement of profit and loss. The derivatives will have to be shown as financial assets or financial liabilities on the balance sheet, as the case may be, as per the requirements of the accounting standard.

Corporate Debt Market

Though the primary market mobilisations through bonds were lower in April at Rs 3,487 crore than those in March at Rs 6,165 crore, they were higher than those raised in April 2007 at Rs 1,300 crore. With the increased interest rate uncertainty, the some of the issuers preferred to wait and watch the RBI's interest rate stance before tapping the market and some of them have tapped the market and have kept their issues open for subscriptions for longer durations so as to attract adequate investor attention (Table 10.6).

The government has finalised norms to enhance the tradability of domestic convertible bonds by allowing the investors to trade equity options separately; this would increase the attractiveness of the domestic bonds both for issuers as well as investors.

In a conference organised by the Asian Development Bank and ICRA, Dr Patil, chairman of Clearing Corporation of India Limited (CCIL), said that price discovery was still not transparent in bond market and there is a lot of manipulation in bond pricing.

Exchangeable Bonds

The exchangeable bonds (FCEBs) proposed by the government as an additional instrument for fund-raising by companies overseas may again be put on the backburner. While the government has already issued the required notification to make the scheme operational, the Reserve Bank of India (RBI) is still not in favour of the instrument. In response to the Budget announcement on exchangeable bonds in 2007-08, RBI has sent a cautionary note to the government stating that the rules for exchangeable bonds will have to be aligned with the norms for external commercial borrowings (ECBs). It had specifically raised issues on transparency on the end use of such funds, which will be raised by one entity and used by another. The guidelines issued by the government are silent on the monitoring of

the end use of funds. There were also issues on monitoring of the foreign direct investment (FDI) cap on companies when bonds raised by one company got converted into another. While monitoring of the FDI cap is done by RBI, in case of exchangeable bonds, RBI had suggested a framework through which the cap could be monitored automatically if an investor converted the shares.

Table 10.6: Profile of Major Commercial Bond Issues During April 2008.

Sr No	Issuing Company / Rating	Nature of instrument	Coupon in percent per annum and tenor	Amount in Rs. crore
	FIs / Banks			
1	NABARD by AAA Crisil, Care	NCD	9.25 per cent with a step up of 20 bps for 3 years with put and call at the end of 2nd year	200
2	IDFC Ltd AAA by Icra, Fitch	Bonds	9.30 per cent with a step up of 202 bps over MIOR for 2 years	185
	NBFCS			
1	ICICI Home Finance Ltd AAA by Icra, Care	Bonds	9.50 per cent for 18 months	100
2	LIC Housing Finance Ltd AAA by Crisil, Care	Bonds	9.70 per cent for 5 years	150
3	Kotak Mahindra Prime Ltd AAA by Crisil, Icra	Bonds	10.40 per cent for 126 months	25
	State Undertaking			
1	Punjab State Electricity Board A-(so) & BBB+(so) by Icra, Care	Bonds	9.40 per cent for 10 years	250
	Central Undertaking			
1	Indian Oil Corp Ltd NA	Special Bonds	7.33 per cent, 8.13 per cent, 8.20 per cent & 8.40 per cent for 1yr, 13 yrs, 15 yrs & 18 yrs respectively	2277
	Corporates			
1	Tata Power Company Ltd AA Crisil, Icra	Bonds	10 per cent with a step up of 10 bps for 10 years	300
			Total	**3487**

Total for April-08 (a year ago): Rs 3995 crore. Total for March-08 (a month ago): Rs 6,784 crore
The amount shown in brackets above denotes the greenshoe option of the issue.
Source: Various Media Sources

Power Bond Trading

The RBI has permitted transfer of trading in the Power Bonds maturing on October 1, 2012 and April 1, 2013, issued by various states to Central Public Sector Undertakings (CPSUs) in terms of Tripartite Agreement among 27 State Governments, Ministry of Power, Government of India and the Reserve Bank of India under One Time Settlement Scheme for dues of State Electricity Boards with effect from April 1, 2008. These bonds were envisaged to be released for trading in a phased manner, as provided in the Tripartite Agreement. Eight

bonds maturing on October 1, 2008, April 1, 2009, October 1, 2009, April 1, 2010, October 1, 2010, April 1, 2011, October 1, 2011 and April 1, 2012 have already been made tradable.

Asian Development Bank (ADB) Report

As per the ADB's report, India's corporate bond market remains underdeveloped despite strong economic growth and significant financial system reforms. The observations are a part of the recently released edition of Asia Bond Monitor, a semi-annual publication, which includes a theme chapter on Indian bond market. The report stated that corporate borrowers continue to depend on bank loans, equity markets and private placement to meet their requirement of funds. To address the lack of liquidity in the bond market, the report suggested easing investment mandate on contractual savings institutions, developing derivative and swap markets and facilitating foreign investment by relaxing exchange controls. The report also advised reforming the stamp duty structure and revamping disclosure requirements for corporate public offers.

4. Government Securities Market

i) Primary Market

Central Dated Securities

Table10.7: Details of Central Government Market Borrowing

(Amount in Rs Crore)

Date of Auction	Nomenclature of Loan	Type of Auction	Notified Amount	Competitive Bids Received		Competitive Bids Accepted		Indicative YTM at cut-off price (in per cent)	Devolvement on Primary Dealers (Rs crore)
				Number	Amount	Number	Amount		
11-Apr-08	7.38 per cent 2015	Normal	6000	222	11114	156	5985	8.14 per cent (Rs.95.83)	NIL
11-Apr-08	7.95 per cent 2032	Normal	4000	241	11995	36	3981	8.67 per cent (Rs. 92.63)	NIL
21-Apr-08	per cent 2018	Normal	6000	354	20964	109	5985	8.24 per cent	NIL
21-Apr-08	8.33 per cent 2036	Normal	4000	254	12741	61	3990	8.77 per cent (Rs. 95.44)	NIL
10-Apr-08	6.57 per cent 2011	MSS	5000	130	6360	97	4998	9.95 per cent (Rs. 96.52)	NA
16-Apr-08	6.57 per cent 2011	MSS	3000	180	7217	57	2998	8.08 per cent (Rs.96.20)	NA
30-Apr-08	6.57 per cent 2011	MSS	3000	123	9073	10	2997	7.87 per cent (Rs.96.76)	NA

Source: RBI Press Releases NA: Not Applicable

As per the scheduled calendar for dated securities, the central government tapped the market twice to mobilise an aggregate amount of Rs 20,000 crore through two instances.

To make the government borrowing programme attractive in times of rising interest rates, the RBI has mooted the introduction of floating rate bonds (FRBs). Usually, banks and primary dealers shun securities in a rising market because a rise in yields means fall in price of the bonds and results in a loss of value. Dealers say that an FRB carries a variable coupon unlike fixed rate government bonds. These variable coupons are pegged as a spread over a fixed rate like that of the 364-day T- bill or current market yield of the benchmark ten-year bond. The Clearing Corporation of India (CCIL) is working on a new issuance and auction format structure for FRBs which is being inbuilt into the NDS current auction format. The auction format will also help price FRBs in the secondary market.

On April 22, four state governments tapped the market to mobilise an aggregate amount of Rs 2,648 crore through a yield-based auction using multiple price auction method and the yield were set in the range of 8.50-8.60 per cent as against a range offered on same maturity of 8.28-8.70 per cent in the previous month.

Treasury Bills

Given the surfeit of liquidity, the RBI resumed MSS absorptions under TBs. However, in the case of 91-day and 182-day bills, RBI rejected the MSS issue size to contain the rise in yield rates under each auction. Thus, as against the notified amount of Rs 22,000 crore, the RBI mopped up only Rs 17,500 crore during the month. As a result, there was a sharp jump in the yields set across TBs and the yield spread between 364-day and 91-day TBs which was 9 basis points in March widened to 34 basis points in April (Table 10.8).

Table 10.8: Auctions of Treasury Bills

(Rs crore)

Date of Auction	Date of Issue	Notified Amt	Bids Received			Bids Accepted			Weighted Avg. price	Implicit Yield
			No.	Total Face Value		No.	Total Face Value			
				Competitive	Non-Competitive		Competitive	Non-Competitive		
91-Day Treasury Bills										
2-Apr	4-Apr	500	49	2633	4500	3	500	4500	98.3	6.94
9-Apr	11-Apr	6000	135	8076	2422	113	6000	2422	98.27	7.2274
16-Apr	18-Apr	5500	117	7913	-	56	3000	-	98.2	7.4353
23-Apr	25-Apr	2500	106	6747	500	40	2500	500	98.19	7.4353
182-Day Treasury Bills										
2-Apr	4-Apr	500	52	2095	-	2	500	-	96.56	7.19
16-Apr	17-Apr	3000	77	2663	1500	28	500	1500	96.38	7.60
364-Day Treasury Bills										
9-Apr	11-Apr	2000	95	4698	-	44	2000	-	93.18	7.37

23-Apr	25-Apr	2000	102	4735	-	55	2000	-	92.92	7.69

Source: Weekly Statistical Supplement, RBI

ii) Secondary Market

Ahead of the announcement of the annual credit policy and the looming inflationary concerns in conjunction with surplus liquidity, spurred fears of monetary tightening; as a result, the market sentiments were subdued. Consequently, the weekly average secondary market turnover ranged between Rs 13,085 crore and Rs 28,392 crore as against a range of Rs 9,038 crore to Rs 28,048 crore in March.

After witnessing a drastic fall in bond prices over the past one month, the bond market finally had some reason to cheer. Following the RBI's decision during the monetary policy on Tuesday, bond yields dropped 20 basis points from an intra-day high of 8.14 per cent to 7.94 per cent on Tuesday. Market players who expected an increase in interest rates during the monetary policy were quite thrilled as the apex bank left interest rates unchanged in its policy review, instead raised banks' reserve requirement (cash reserve ratio from 8 to 8.25 per cent with effect from May 24) to tame inflation.

Table 10.9: Inter-Category Wise NDS Reported Outright Trade of Central Govt (Buy side) Mar 2008

Buyer Category	Sellers									Total	Per cent of total market share
	Foreign Banks	Public Sector Banks	Private Sector Banks	Primary Dealers	Ins. Cos	Coop Banks	Mutual Funds	Others	FIs		
Foreign Banks	53.93	14.86	6.77	14.77	3.65	4.28	1.73	0.00	0.00	100	43.48
Public Sector Banks	32.72	8.35	20.26	21.06	13.28	1.12	3.21	0.00	0.00	100	17.31
Private Sector Banks	31.43	16.68	20.38	21.38	3.60	3.15	2.80	0.56	0.04	100	12.64
Primary Dealers	65.29	9.20	15.86	5.12	0.22	1.50	1.73	1.08	0.00	100	11.20
Ins.Cos	19.53	0.00	34.45	46.03	0.00	0.00	0.00	0.00	0.00	100	8.67
Coop Banks	61.92	8.06	9.29	7.41	1.54	6.57	5.11	0.11	0.00	100	3.32
Mutual Funds	19.19	12.12	11.11	48.48	1.01	4.04	4.04	0.00	0.00	100	2.40
Others	0.00	66.14	30.10	3.76	0.00	0.00	0.00	0.00	0.00	100	0.99
FIs	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100	0.00

Source: CCIL Rakshitra – April 2008

On April 16, 2008, SEBI decided to allow mutual funds to sell government securities contracted for purchase in the DVP-III mode. The SEBI board approved net settlement in government securities by mutual funds according to the guidelines issued by the RBI and also their participation in the when issued market. Under the net settlement, it is possible to sell debt market securities without actually giving delivery provided the transaction is guaranteed

by Clearing Corp of India. Taking a step forward towards development of the domestic debt market, the SEBI brought mutual funds on a par with primary debt dealers, banks and insurance companies

As per the inter-category data published by CCIL for NDS reported trades, foreign banks have been the dominant players in dated securities reported on the NDS platform of the RBI, followed by public sector banks (Table 10.9).

Money Market

The short-term money market rates remained stable in April and hovered around the floor rate set by the reverse rate of 6 per cent due to huge surfeit of liquidity despite looming uncertainty given the heightened inflationary conditions. Even the hike in CRR of 25 basis points effective from April 26 had marginal impact on call rates, unlike in November 2007 when the CRR was hiked by 50 basis points and the short-term rates had firmed up. Yet, the volatility in call rates, as defined by the measure of standard deviation, was higher in April than that in March

The call rates showed distinct stability as compared with Collaterlised Borrowing and Lending Obligation (CBLO) and repo rates which were volatile, as they dipped to near 1 per cent on a few occasions and then peaked over 6.5 per cent; such vast variations in the rates of these segments implies limited arbitrage opportunities between these segments as mutual funds, who are the main lenders, deploy huge funds in the collateralised segments but they do not operate in the call market.

The collateralised segment is the dominant segment of the money market and it accounts for 80 per cent of the total volume. In both the CBLO and market repo sub-segments, mutual funds have been the major lenders of funds while commercial banks and primary dealers have been the main borrowers (Table 10.10).

Table 10.10: Comparison of Call, Overnight CBLO and Repo rates

Week Ending	Weighted Average Rates (in per cent)			Daily Average Volumes (Rs. crore)		
	Call	Overnight CBLO	Repo	Call	Overnight CBLO	Repo
4-Apr-08	6.99	5.46	6.50	9623	33699	9567
11-Apr-08	5.61	3.48	4.28	7540	37999	17408
17-Apr-08	6.14	6.00	6.09	10998	35382	12357
25-Apr-08	6.09	5.40	5.87	12847	38325	15884

Source: CCIL Weekly Updates, Various Issues

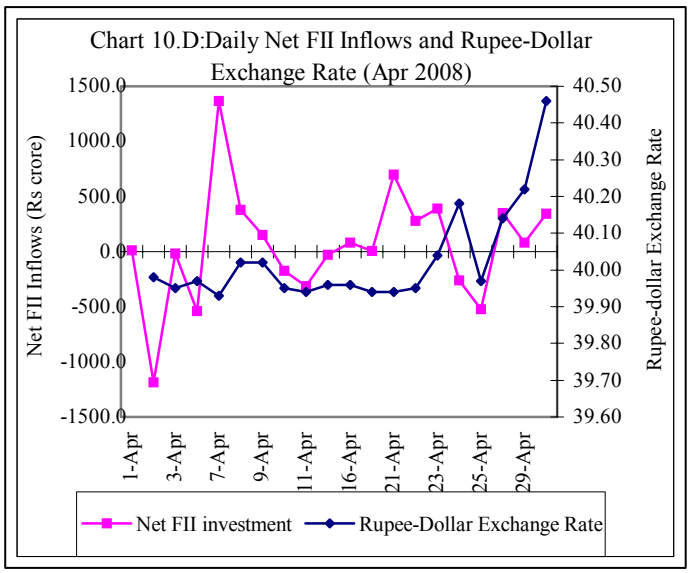
Reverse Repo and Repo under RBI's LAF

Table10.11: Repo/Reverse Repo Amount Tendered under RBI's LAF					
(Amount in Rs Crore)					
Week	Repo		Reverse Repo		Outstanding Amount
	Tendered	Accepted	Tendered	Accepted	
Jan-08	37135	37135	393350	393350	356215
Feb-08	175765	175765	170345	170345	-5420
Mar-08	223795	223795	158940	158940	-64855
Apr-08	400	400	566830	566830	566430
Source: RBI Weekly Statistical Supplement (WSS)					

With a significant improvement in the liquidity conditions mainly due to substantial reduction in cash balances of the central government, the return flow of advance tax payments and coupon and redemptions related inflows, the size of reverse repo bids under LAF window jumped to about 9-month peak of Rs 79,005 crore on April 8. Despite the various measures undertaken by the RBI to moderate the building liquidity, the size of reverse repo bids continued to remain sizeable. After dipping to Rs 7,045 crore on April 17 following the announcement of the CRR hike, it again rose to a high of Rs 39,705 crore on April 22. However, after April 26 when the 25 basis points hike came into effect, the size of bids dipped to Rs 4,270 crore on April 30, but again rose to Rs 20,250 crore on May 2. There was only one repo bid tendered and accepted during the month on April 2 of Rs 400 crore (Table 10.11).

Foreign Exchange Market

In April, the rupee-dollar exchange rate depreciated by 36 paise over the previous month, despite lower foreign currency inflows; given the increased demand for dollars from oil-importing companies after the sharp surge in international crude oil prices following unrest in one of the major oil exporting countries (Chart 10.D). With the domestic inflation ruling at high levels above 7 per cent, there was expectation that the RBI would allow the rupee to appreciate as an instrument to arrest



inflation by restricting the import of global inflation into the domestic economy. Further, as domestic equity markets enjoyed a recovery phase, the rupee appreciated but the RBI intervened to contain the appreciation of the rupee. But, as the oil-related demand for dollar increased, the rupee began depreciating which provided an opportunity to the exporters to bring in their receivables.

There has been a massive expansion in the forex market turnover in the recent period. The average daily turnover in the foreign exchange market increased to $ 48.1 billion during 2007-08 from $ 25.7 billion in 2006-07, reflecting large cross-border trade and capital flows. While average inter-bank turnover increased to $ 33.8 billion from $ 18.7 billion in 2006-07, merchant turnover increased to $ 14.3 billion from $ 7.0 billion. The ratio of inter-bank to merchant turnover was 2.36 during 2007-08 as compared with 2.67 a year ago.

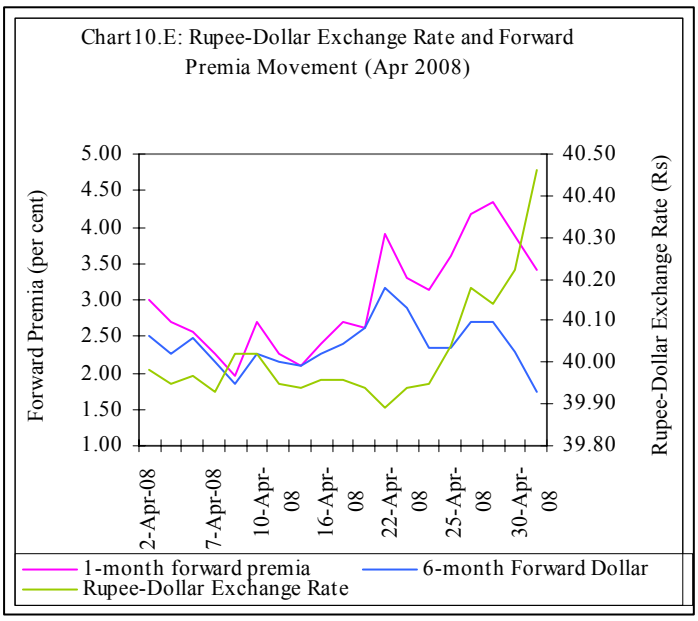
As shown in table 10.12, the Indian rupee has depreciated from Rs 39.97 on March 31,2008 to Rs 40.46 on April 30,2008, while it has appreciated over previous year (at Rs 41.07 on April 27,2007). While Chinese Yuan over the period has appreciated from 5.564 to 5.324 but depreciated to 5.695 on March 31, 2007.

10.12: Exchange Rate for Rupee.					
Countries	27-Apr-07	30-Apr-08	31-Mar-08	Apr / Mar %Change	2008-09 %Change
Euro	56.032	62.875	63.201	0.518	-10.884
Japanese Yen*	34.339	38.874	39.930	2.717	-11.665
British Pound	82.083	79.577	79.480	-0.121	3.149
US Dollar	41.070	40.460	39.970	-1.211	1.508
Argentine Peso	13.266	12.790	12.641	-1.164	3.721
Australian Dollar	33.883	37.778	36.692	-2.872	-10.310
Brazilian Real	20.304	23.730	23.446	-1.199	-14.440
Canadian Dollar	36.824	40.079	38.885	-2.979	-8.122
Chinese Yuan	5.324	5.780	5.695	-1.476	-7.884
Danish Krone	7.521	8.426	8.476	0.588	-10.740
Indonesian Rupiah*	0.452	0.438	0.434	-1.029	3.116
South Korean Won*	4.423	4.047	4.030	-0.414	9.292
Malaysian Ringgit	12.004	12.812	12.540	-2.125	-6.304
Mauritian Rupee	1.301	1.560	1.538	-1.376	-16.599
Nepalese Rupee	0.628	0.627	0.625	-0.439	0.187
New Zealand Dollar	30.400	31.340	31.716	1.199	-3.000
Norwegian Krone	6.885	7.885	7.850	-0.443	-12.680
Pakistan Rupee	0.676	0.627	0.637	1.635	7.846
Singapore Dollar	27.079	29.708	28.966	-2.500	-8.853
South African Rand	5.876	5.327	4.935	-7.370	10.293
SriLanka Rupee	0.373	0.375	0.371	-1.145	-0.521
Swedish Krona	6.109	6.735	6.718	-0.256	-9.289
Swiss Franc	34.032	38.956	40.215	3.232	-12.640
Thai Baht	1.180	1.275	1.270	-0.341	-7.415
U.A.E.Dirham	11.183	11.017	10.884	-1.211	1.508
Venezuelan Bolivar	0.019	0.019	0.019	-1.211	1.508
Hongkong Dollar	5.251	5.192	5.136	-1.079	1.142

Source: - www.imf.org/external/np/fin/data/param_rms_mth.cfm
Argentine Peso & Hongkong dollar: - www.fxstreet.com
* For 100 units

With the RBI being active in the forward market, the forward premia firmed up across maturities. As the spot rupee depreciated, the exporters began bringing in receivables, but as the international crude oil prices were ruling at high levels, importers began covering their positions, particularly in the short-term. Among the three tenures, the one-month premia ruled higher than the three and six-month premia against the backdrop of sharp surge in global crude oil prices, implying that the market expected the rupee to depreciate more in the short-term than in the long term (Chart 10.E).

Currency Derivatives



According to the earlier mentioned Rajan committee said that, restricting inflows of foreign funds is not an effective solution in the long run to prevent the local currency from strengthening that is reducing export competitiveness. The committee is of the view that foreign investment should be utilised in areas where the country needs it most. This would encourage domestic investors to take interest in those areas, creating a virtuous cycle. It also feels the central bank should focus

primarily on inflation control and should be willing to revise interest rates whenever needed. The committee said that exchange-traded currency derivatives in all currencies with rupee settlement to be traded on NSE and BSE Exchange-traded interest rate derivatives using both cash settlement and physical settlement with trading on NSE and BSE.

Also, the RBI has announced the introduction of currency futures on eligible exchanges. The central bank has, in principle, allowed banks and brokers as the first participants to start currency futures on eligible exchanges. As regards companies, the RBI has clarified that corporates accessing such products should make compulsory disclosures of unhedged exposures and hedging in their annual accounts. The companies can use such products only if they have an underlying rupee dollar positions or trades. The RBI is of the view that banks, being regulated entities, will be allowed both as trading cum clearing members of their own account and clients account and also as professional clearing members to provide liquidity in the market. Brokers could be allowed on basis of multiple criteria like net worth, market reputation, regulatory framework, and participation in the derivative segment.

The total forex settlement volume on CCIL has increased both in rupee as well as dollar terms; it has risen to Rs 12,69,788 crore in February from Rs 11,36,947 crore in January and in dollar terms, it has increased to US $ 317,691 million from US $ 286,379 million (Table 10.13). The daily average turnover has risen to $ 15.8 billion from Rs 13.6 billion, during the same period.

Commodities Futures Market

With the inflation rate hovering over 7 per cent in recent weeks, the government is looking at more subtle measures to control prices even after a slew of duty cuts and price control measures. Amid fears that the central government may ban futures trading on agri commodities as part of its ongoing battle against inflation, the volumes of these commodities on MCX and NCDEX have declined. The total turnover has declined to Rs 337,814 crore in April as against Rs 470,141 crore in March, a fall of about 28 per cent; yet, the turnover has been higher than that recorded in April 2007 at Rs 311,825 crore. Similarly, the turnover on MCX has declined from Rs 360,120 crore in March 2008 to Rs 279,581 crore in April 2008 and that on NCDEX has fallen from Rs 87,772 crore to Rs 47,351 crore.

In line with a slew of fiscal measures taken by the government to check inflation, both the RBI and the FMC have got into action. In an attempt to curb hoarding of essential

commodities, RBI has advised banks to review their advances to traders as also advances against warehouse receipts. The RBI has further advised them to exercise caution while extending such advances to ensure that bank finance is not used for hoarding. Meanwhile, FMC has already alerted commodity exchanges to report quotes and trading patterns of illiquid contracts on the futures market.

With the rising steel prices, there has a vociferous demand for reclassification of steel and its products under Essential Commodities Act, 1955 a year after it was declassified from the list of essential commodities. The Act gives essential commodities at a fair price and gives power to the government to control production, supply and distribution of steel and its products.

Table 10.14: Monthly Turnover Of Commodity Exchanges

(Amount in Rs. crore)

SR No	Commodity Exchange	April-07 Turnover	Feb-08 Turnover	Mar-08 Turnover	Apr-08 Turnover
1	Multi Commodity Exchange of India Limited, Mumbai (MCX)	203840 (65.4)	347539 (79.9)	360120 (76.6)	279581 (82.8)
2	National Multi-Commodity Exchange of India imited, Ahmedabad (NMCE)	3291 (1.1)	1833 (0.4)	7627 (1.6)	3858 (1.1)
3	National Commodity & Derivatives Exchange Ltd. Mumbai (NCDEX)	49721 (15.9)	69234 (15.9)	87772 (18.7)	47351 (14.0)
4	Chamber of Commerce, Hapur	2010 (0.6)	1446 (0.3)	1075 (0.2)	1057 (0.3)
5	National Board of Trade, Indore (NBT)	7679 (2.5)	10959 (2.5)	8994 (1.9)	4955 (1.5)
	Total *	311825	434756	470141	337814

*: Total includes the monthly turnover of the remaining 18 commodity exchanges .
Figures in brackets denote percentage change in total turnover
Source: FMC. (www.fmc.gov.in)

Commodity-wise Turnover

Table10.15: Commodity-wise turnover				
Commodity	March-08		April-08	
	Trading On all Exchanges (Rs. Cr)	Percentage To total Turnover	Trading On all Exchanges (Rs. Cr)	Percentage To total Turnover
Metal				
Gold	141857	30.2	104509	30.9
Silver	92168	19.6	64540	19.1
Copper	33871	7.2	35518	10.5
Zinc	16731	3.6	10364	3.1
Nickel	4713	1.0	2368	0.7
Lead	6616	1.4	4494	1.3
Crude Oil	52754	11.2	54466	16.1
Agricultural Products				
Pepper	4808	1.0	2365	0.7
Jeera	2050	0.4	2528	0.7
Soy oil	34644	7.4	16236	4.8
Gaur seed	13951	3.0	6792	2.0
Chana	14070	3.0	8448	2.5
R/M seed	12472	2.7	9272	2.7
Soy Bean	8091	1.7	4344	1.3
Turmeric	3029	0.6	2689	0.8
Source: FMC (www.fmc.gov.in)				

Among the major agricultural commodities, except for jeera, there has been a sharp decline in the turnover; in some cases, the volumes have nearly halved to that in March. The trading in soya oil has dipped from Rs 34,644 crore in March to Rs 16,236 crore in April. Similarly, the trading in chana has slipped from Rs 14,070 crore to Rs 8,448 crore over the same period (Table 10.15). With the sharp rise in precious metals, the volume of trade has declined. The trading in gold has declined from Rs 141,857 crore in March to Rs 104,509 crore in April and that in silver has dipped from Rs 92,168 crore to Rs 64,540 crore.

Commodity Transaction Tax (CTT*)*

Though there has been extremely vocal opposition to the imposition of commodities transaction tax (CTT) from commodity exchanges, traders and even the commodities regulator has supported them in opposing the CTT. According to FMC Chairman B C Khatua, the CTT, which has been proposed by finance minister P Chidambaram, in his budget speech, could divert volumes from domestic commodity exchanges to foreign platforms and may lead to a flourish in dabba trading. As per his views, domestic traders have now moved to foreign platforms. Wheat turnover has not switched to other commodities but has migrated overseas, especially to the Chicago Board of Trade (CBOT). He opined that commodity futures trade in India is not matured enough to accept the CTT as the volume on domestic platforms is less than 5 per cent of the total output of major commodities in the country. Senior officials at the Multi Commodity Exchange (MCX), the country's largest commodity exchange, also feel that big corporates, of late, have started entering the domestic platform because of the opportunity and low transaction cost.

The Prime Minister's Economic Advisory Council, headed by C Rangarajan. Prime Minister Manmohan Singh has asked the council to review the proposal, announced in the

2008-09 Union budget, following representations from industry and FMC. The council has submitted its report to the prime minister, recommending a partial withdrawal of CTT, saying that the new tax would be detrimental to commodities trading, which is still in its nascent stage.

Despite such vociferous opposition to CTT especially from the two major commodity exchanges, the Finance Minister has said in the Rajya Sabha that despite intense lobbying against the CTT and immense pressure being exterted on him for its withdrawal, he has said that CTT is to remain.

The Grain Situation

According to a recent report of the International Grain Council (IGC), the world wheat production would be at 646 million tonne (mt), an increase of 42 mt over the previous year, due to a 2.5 per cent increase in the area under cultivation. The global prices of maize were around $240 a tonne by March 27. The IGC forecasts global maize output to decline by 20 mt to 748 mt. Barley output would increase 10 per cent to 148 mt. According to the official estimate, India has achieved record grain production of 219.32 mt in 2007-08, including 94.08 mt of rice, 74.81 mt of wheat, 36.09 mt of coarse cereals, and 14.34 mt of pulses. The cotton output is estimated at 23.38 million bales of 170 kg each, an all-time record. The oilseeds output is estimated at 27.16 mt. Despite the good production, there is a deliberate manipulation of food prices both at the global and at the domestic levels.

Improving the Infrastructure

According to FMC Chairman B C Khatua, a uniform tax structure and free movement of goods throughout the country were critical to the growing significance of spot trade in India. Spot exchanges are unlikely to succeed in the present framework of state and central levies, which vary from state to state and commodity to commodity. So far, two national commodity exchanges - the Multi Commodity Exchange (MCX) and the National Commodity & Derivatives Exchange (NCDEX) - have obtained clearances from a number of states to launch spot online trade and are in the process of facilitating trading in various commodities soon. Presently, spot trade in India is largely fragmented due to poor infrastructure and lack of state government interest. The Agriculture Commodity Marketing Committee (APMC) Act regulates spot trade in the country and the Act differs from one state to the other. Some states, including Bihar and Kerala, have scrapped the APMC Act long ago

and spot trades in these states are largely controlled by local aaratias and prices are determined by the demand-supply situation on a daily basis.

Measures to Widen Market

The Planning Commission appointed High Level Group on Services recommended for allowing banks to participate in the commodity derivatives market to bring depth and liquidity. Currently, banks are not permitted to participate in both commodity derivatives and equity derivatives market. The Panel has also suggested that the Government may consider allowing banks to participate in equity derivatives market as it would help them better manage risks in their equity portfolios and would also enhance market liquidity.

Carbon Trading

The National Commodity and Derivatives Exchange (NCDEX), India's largest agri-trading platform, has announced the launch of the futures contract in certified emission reduction (CER), a type of carbon credit certificate futures contract. The contract will be launched on April 10 for delivery in December 2008. The trade size in each lot has been fixed at 500 CERs and a client wise limit is fixed at 11,000 lots. The CER contract on NCDEX will help domestic carbon credit generators with better realisations as they sell CERs at 80 per cent discount on European trading platforms. After China, India is the largest supplier of CERs. India is expected to account for 14.69 per cent of the expected annual number of CERs from the registered projects under the clean development mechanism (CDM) of the United Nations Framework Convention on Climate Change (UNFCCC) by 2012. NCDEX Spot Exchange (NSEL) is set to begin spot trade in coffee, steel ingots, sugar and soybean by month-end.

NCDEX has recorded total volumes of Rs 174.66 crore in the first fortnight of trading in certified emission reduction (CER). The total number of CERs traded contracts was 3,396 during this period, making the exchange one of the largest in the world in CERs. NCDEX is the first exchange in any of the developing countries of the world to launch a futures contract for carbon credit issued under United Nations Framework Conventionon Climate Change on its exchange platform. The CER contract is available for delivery in December 2008. The CERs contracts launched on April 10 has witnessed significant trading interest. The subsequent yearly contracts are likely to be launched within two months for deliveries in December between 2009 and 2012

Market Ownership

The commodity market regulator Forward Markets Commission (FMC) may cap the single domestic entity ownership below 26 per cent to avoid dominant control by any single owner. The cap is 5 per cent in stock exchanges but there is no such limit at present in commodity bourses. According to sources, this will result in strategic participation by investors, who will exit for a better valuation. The single entity limit for stock exchanges cannot be replicated for commodity exchanges since they are in the early stages of development.

Findings of a Research report

After a strong beginning in 2008, prices of industrial commodities, barring crude oil, were expected to cool down in the second half of the year. According to data compiled by the Economist Intelligence Unit (EIU), a London-based research agency, the prices of base metals are likely to fall 1.5 per cent as against a growth of 10.5 per cent last year. According to EIU estimates, the Industrial Raw Materials (IRM) price index will rise by an average of 1.1 per cent in 2008 despite spot prices of major raw materials, including coke, copper concentrates, alumina, iron ore, ferro allows, having nearly doubled in the last one year.

Abhijit Sen Committee

The five-member Abhijit Sen committee on futures trading has submitted its long-awaited recommendations to the government on April 29 2008; it has said that it is difficult to establish that futures trading of agricultural commodities affect spot prices. Sen further said that "this committee is not in the business of recommending lifting or imposing a ban on futures trading. Explaining the dilemma the panel faced with regard to the data it had analysed, Dr Sen said, “It is virtually impossible to make any statement either this way or that way which would be acceptable to everyone” and further said that they were not giving any unanimous view on the subject. Thus, the panel has not recommend a ban on futures trading, but wanted the existing temporary suspension of futures trading in wheat, rice urad and tur to continue for some time. The panel suggested strengthening of FMC and the commodity exchanges to deal with proper functioning of futures trading in a transparent manner. The panel report has also said that statistically there was no perfect model to find the linkage between futures trading and the present situation of rise in prices of essential commodities.