

CHAPTER 2

DOMESTIC SOURCES OF FINANCE AND INTERNATIONAL FINANCIAL MARKET : EURO ISSUE AND ADR, GDR

Broadly speaking, the long-term sources of finance can be classified into debt and equity. Although the distinction between debt and equity is often made in terms of bonds and shares, its roots lie in the nature of the cash flow claims of each type of financing. The debt and equity may be differentiated as follows:

Imp 3. **Zero-Interest Fully Convertible Debentures (ZFCD):** In this case, the debenture is compulsorily fully convertible into equity shares at the expiry of a given period (not exceeding 3 years) from the date of issue. For the intervening period, no interest is payable by the company to the debenture holder. The return to debenture holders is available in the form of difference between the issue price of the ZFCD and the market price of the converted shares. Though, the ZFCD are ultimately to be converted into equity share capital, yet, if the period of conversion is after 18 months from the date of issue, then as per the SEBI Guidelines, the issue of ZFCD must be credit rate by an approved credit rating agency. In case of ZFCD, the debenture holders are not given any option and are compulsorily converted into equity share capital. Mahindra and Mahindra Ltd. and Indian Rayon and Industries Ltd. has issued ZFCD. → Compulsory Convert after 3 years (interest 0%)

SPN is a **hybrid security** i.e. it combines both features of equity and debt products.

The **conversion of detachable warrants into equity** has to be done **within the specified time**.

After the **lock-in-period**, the holder has an option to **sell back the SPN to the company at par value**.

In case the holder keeps his investment further, he is **repaid the principal amount along with the additional interest/premium on redemption in installments**.

TISCO (tata iron & Steel Company) took the lead in July, 1992 by making a mega rights issue of equity shares and secured premium notes.

Imp.

5. Deep Discount Bonds (DDB): A DDB is also a type of a zero interest bond. But is not convertible. It has got a face value but the issue price of the DDB is a discounted value. The DDB is redeemed at the expiry of a specified period at the face value. The return to the DDB holders is available in the form of difference between the issue price and the realizable maturity value. There is no coupon rate and no interest is payable during the life of the DDB. The Industrial Development Bank of India issued in 1992, DDB of the face of Rs.1,00,000 redeemable in 25 years. The issue price was however, Rs.2,700 and the investor were given option to get redemption at the end of 5th, 10th, 15th and 20th year at different values. If an investor holds the DDB for full 25 years, then the rate of return comes to about 15.5%. since then SIDBI, ICICI and IFCI have also issued DDB of different denominations and maturities.

→ heavily discount से issue के maturity पर face value मिलेगा Investor को ।

Private Equity



Foreign Capital:-

Foreign capital refers to capital fund provided by foreign institutions, foreign investors, foreign banks, etc. it includes all types of flow of capital funds from overseas capital markets to local industries. Foreign funds can be relied to supplement the domestic savings and to provide superior physical and managerial technology. However, foreign capital has its own merits and demerits. It involves not only financial and economic considerations, but in a wider sense, also affect the sovereignty, dependency, economic and political volatility of a country. The countries have been cautious in allowing the foreign capital to enter the industrial scene of that country. In India, the foreign capital had remained subdued till 1990. There were several regulations and constraints applied by the Government on the inflow of foreign capital in India. However, with the onset of process of liberalization and globalization, the Government started relaxing, with supervision and control, the inflow of foreign capital in India. Number of policy measures have been introduced to attract foreign investment and the foreign investors, individual as well as institutional.

The inflow of foreign capital is determined not only by the economic policies of a country, rather there are several other factors affecting the inflow of foreign investment. Some of these factors are relative interest rates, relative rates of inflation, Government policies, political conditions, country rating, currency convertibility etc.

Forms of Foreign Capital. The sources from where foreign capital can be raised can be grouped into two: official and private. The official sources include loans, aids, grants, gifts, etc., by one Government or Government agency to another country. The official sources may also be in terms of loans at concessional rates with longer maturity and liberal repayment schedules.

Private foreign capital is available from the individual and institutional investors. This capital is available on pure commercial terms. Broadly, there are two forms in which the private capital may flow: Direct Foreign Investment (DFI) and Portfolio Investment. DFI is one where the foreign investor establishes and does business in a country. In case of portfolio investment, the foreign funds flow in terms of subscription to securities or direct lending. In India, the portfolio investment is made through Euro Issues, External Commercial Borrowings, Stock Market Transactions, etc.



FCCB



- ✓ Foreign Currency convertible bond issued by a country in a currency different than the its own currency
- ✓ Powerful instrument by which the country raises the money in the form of a foreign currency
- ✓ Bond acts like both a debt and equity instrument
- ✓ Bondholder the option to convert the bond into a company's equity share
- ✓ Retain all features of a convertible bond

FCEB

..... *stands for*

Foreign Currency Exchangeable Bonds

2) Foreign Currency exchangeable bonds & —

