Drawbacks of SEBI’s Rule

Why in news?

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Securities and Exchange Board of India is planning to make new changes in the bond market.

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What are the difference between Bond market and Banks?

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- In the bank-based system, banks play a dominant role in mobilising savings, allocating resources among the various sectors of the economy and regions of a country, and providing risk management facilities.
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- Developed countries such as Japan, Germany, France and Italy and developing countries such as Argentina, China, India and Pakistan follow Bank based system.
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- In a market-based system, the intermediary role of banks is reduced to a great extent and the investors or the savers directly park their funds with the borrowers (corporates).
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- Developed countries such as US, UK, Singapore and Korea and developing countries such as Brazil, Mexico and Turkey follow the market-based system.
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- Economists have found that financial systems tend to become more market-based as the economy develops.
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What are the concerns with recent decision of SEBI?

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- **Stringent regulation -** Market regulator makes it mandatory for companies

with over Rs. 100 crore debt and a credit rating of ‘AA and above’ to compulsorily raise 25 per cent of their debt from the bond market.
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- The move seems to be a premature one, Instead of allowing the market to function on its own based on demand and supply, there seems to be an effort to arm-twist firms to go in for a particular type of financing.
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- **Investor’s attitude -** Indian savers find it comfortable to lend the funds to banks and pass on the risk management to banks.
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- For this transfer of risk management, they are willing to accept lower return on their funds, Thus forcing depositors to take the market risk will not work out.
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- If the investors shun the equity or bond market, it is because of their risk aversion.
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- **Structural issues -** Given the highly leveraged state of corporates and the banks’ huge NPA problem, it is not good idea expect corporates not to default on bonds on maturity or interest payment.
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- Any default in interest payment by the company will make the bond price plummet in the market and there may not be buyers, which makes liquidity of the bond unreliable.
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What is the way forward?

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- Market participation has to mature on its own over a period and regulators can only provide conducive environment to facilitate that.
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- The basic function of SEBI is to protect the interests of investors in securities market.
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- Thus forced borrowing through bond market cannot be in the interest of the investors or corporates.
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Source: Business Line

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