



# Fixed Income Market

## A Glossary of Terms

No.	Terms	Description
1	<b>Financial System</b>	A system that acts as a mediator to facilitate transfer of money/funds efficiently and timely from ones who have it in surplus to the ones who are in need of it. This transfer happens through agreements called Debt Instruments.
2	<b>Financial Product</b>	When money/fund flows from the entity that has it in surplus to the entity that is in dearth of it, there is a legally binding agreement that is prepared which gives birth to a Financial Product. These are the products through which Corporates/Government raise funds.
3	<b>Financial Product Creation</b>	The process of financial product creation is pretty much like the process of lending and borrowing. <ul style="list-style-type: none"> <li>● In the process, there are usually two parties involved- a lender and a borrower.</li> <li>● There is an obligation or a promise to pay back</li> <li>● A rate of interest is fixed at which the funds are borrowed/lend.</li> <li>● A tenure of repayment for the sum borrowed is fixed.</li> </ul>
4	<b>Collateral/ Guarantor</b>	To avoid a situation wherein a borrower fails/defaults in the payment of the borrowed sum, the concept of Collateral/ Guarantor was brought in.
5	<b>Debt Market</b>	The debt market is the market where Fixed Income Securities of various types and features are issued and traded. Debt Markets are therefore, markets for fixed income securities issued by Central and State Governments, Municipal Corporations, Government Bodies and commercial entities like Financial Institutions, Banks, Public Sector Units, Public Ltd Units and also structured finance companies.
6	<b>Role of debt Market</b>	<ul style="list-style-type: none"> <li>● Efficient mobilization and allocation of resources in the economy</li> <li>● Financing the development activities of the Government</li> <li>● Transmitting signals for implementation of the monetary policy</li> <li>● Facilitating liquidity management in tune with over all short term and long term objectives.</li> </ul>
7	<b>Money Market</b>	The Money market is a general term for the markets in which banks and financial institutions lend to and borrow from each other, trade in financial instruments such as Certificates of deposits, Commercial papers and enter into agreements like Repos.

No.	Terms	Description																	
8	<b>Fixed Income Securities</b>	<p>Fixed Income Securities are often referred to as bonds, fixed income assets which are issued by Corporations, Governments and Federal agencies. These investments provide a steady stream of interest income and the repayment of their principal at the end of a certain period of time.</p> <p>However, their value may fluctuate during the lifetime of the 'loan' resulting in an investment gain / loss.</p> <p>Interest rates and inflation have a very strong influence on fixed income instruments.</p>																	
9	<b>Fixed Income Securities – Features</b>	<ul style="list-style-type: none"> <li>● Fixed Income Securities offer predictable stream of payments by way of interest and repayment of principal at maturity of the instrument.</li> <li>● The debt securities are issued by the eligible entities against the money borrowed by them from the investors in these instruments.</li> <li>● Most debt securities carry a fixed charge on the assets of the entity and generally enjoy a reasonable degree of safety and by way of security of the fixed and/or movable assets of the company.</li> </ul>																	
10	<b>Fixed Income Securities – Why invest?</b>	<ul style="list-style-type: none"> <li>● The investors benefit by investing in fixed income securities as they preserve and increase their invested capital and also ensure the receipt of regular interest income.</li> <li>● The investors can even neutralize the default risk on their investments by investing in Government Securities, which are normally referred to as risk free investments due to the sovereign guarantee on these schemes.</li> <li>● The prices of debt securities display a lower average volatility as compared to the prices of other financial securities and ensure the greater safety of accompanying investments.</li> <li>● Debt securities enable wide based and efficient portfolio diversification and thus assist in portfolio risk mitigation.</li> </ul>																	
11	<b>Different instruments in Debt Market</b>	<table border="1"> <thead> <tr> <th>Market Segment</th> <th>Issuer</th> <th>Instruments</th> </tr> </thead> <tbody> <tr> <td rowspan="2">Government securities</td> <td>Central Government</td> <td>Zero Coupon Bonds, Coupon Bearing Bonds, Treasury Bills</td> </tr> <tr> <td>State Government</td> <td>Coupon Bearing Bonds</td> </tr> <tr> <td rowspan="2">Public Sector Bonds</td> <td>Government Agencies / Statutory Bodies, PSUs</td> <td>Government Guaranteed Bonds, Debentures, PSU Bonds, Commercial Paper</td> </tr> <tr> <td>Private Sector Bonds</td> <td>Corporate, Banks</td> <td>Bonds, Debentures, Commercial Paper, Floating Rate Bonds, Zero Coupon Bonds, Inter Corporate Deposits, Certificates of Deposits</td> </tr> <tr> <td></td> <td>Financial Institutions</td> <td>Certificates of Deposits, Bonds</td> </tr> </tbody> </table>	Market Segment	Issuer	Instruments	Government securities	Central Government	Zero Coupon Bonds, Coupon Bearing Bonds, Treasury Bills	State Government	Coupon Bearing Bonds	Public Sector Bonds	Government Agencies / Statutory Bodies, PSUs	Government Guaranteed Bonds, Debentures, PSU Bonds, Commercial Paper	Private Sector Bonds	Corporate, Banks	Bonds, Debentures, Commercial Paper, Floating Rate Bonds, Zero Coupon Bonds, Inter Corporate Deposits, Certificates of Deposits		Financial Institutions	Certificates of Deposits, Bonds
Market Segment	Issuer	Instruments																	
Government securities	Central Government	Zero Coupon Bonds, Coupon Bearing Bonds, Treasury Bills																	
	State Government	Coupon Bearing Bonds																	
Public Sector Bonds	Government Agencies / Statutory Bodies, PSUs	Government Guaranteed Bonds, Debentures, PSU Bonds, Commercial Paper																	
	Private Sector Bonds	Corporate, Banks	Bonds, Debentures, Commercial Paper, Floating Rate Bonds, Zero Coupon Bonds, Inter Corporate Deposits, Certificates of Deposits																
	Financial Institutions	Certificates of Deposits, Bonds																	
12	<b>Different instruments in Money Market</b>	<ul style="list-style-type: none"> <li>● Call Money</li> <li>● Repo</li> <li>● Government Securities</li> <li>● State Development Loans</li> <li>● Treasury Bills</li> <li>● Certificates of Deposit</li> <li>● Fixed Deposit</li> <li>● Non-Convertible Debentures</li> <li>● Commercial Papers</li> </ul>																	

No.	Terms	Description
13	<b>Call Money</b>	Call Money is basically overnight lending and borrowing at a pre- determined rate at a simple interest for a tenor ranging between 1-7 days. The participants in the same are mainly Banks, All India Financial Institutions, PSUs, Mutual Funds.
14	<b>Repo Rate</b>	The repo rate is simply the annualised interest rate at which banks borrow money from the Reserve Bank of India (RBI) over a short term. This is generally seen as a way of tiding over a short-term liquidity crunch that is experienced by banks.
15	<b>Reverse Repo Rate</b>	A reverse repo is when the RBI borrows money from the bank. The interest rate at which RBI borrows the money becomes the reverse repo rate. While the repo is generally used to infuse liquidity into the system, the reverse repo is used to reduce the supply of money in the market.
16	<b>Government Securities (G Secs)</b>	G Secs are zero credit risk bonds issued by GOI. It is often referred to as sovereign debt.
17	<b>Types of Government Securities (G Secs)</b>	<ul style="list-style-type: none"> <li>● Fixed coupon bearing instruments</li> <li>● Floating or Variable rate bonds with Annual reset</li> <li>● Zero coupon bonds</li> </ul>
18	<b>State Development Loan</b>	These are zero credit risk bonds issued by State Government. They have characteristics similar to Fixed Coupon Central Government Security. They are quite illiquid in nature due to low demand.
19	<b>Treasury Bills</b>	These are short term debt instruments issued by the GOI for a tenor ranging between 91- 364 days. These are zero credit risk instruments which are traded in the secondary market wherein no interim interest payments are made and par value is paid at maturity of the instrument. This is a highly liquid instrument.
20	<b>Certificate of Deposit</b>	These are fixed interest rate and fixed tenor instruments issued by Banks and Financial Institutions. These instruments are normally rated by Rating Agencies so they carry minimal interest rate risk.
21	<b>Fixed Deposits</b>	Fixed Deposits are fixed interest rate and fixed tenor financial instrument issued by banks and financial instruments. These are unrated financial instrument which do not carry any interest rate risk.
22	<b>Non Convertible Debentures (NCDs)</b>	These are bonds issued by banks, financial instruments and corporates with fixed interest rate and fixed tenor. They are rated by rating agencies as they carry significant interest rate and credit risk. NCDs can be traded in secondary market.
23	<b>Commercial Paper (CPs)</b>	CPs are short term papers issued by corporates to meet their working capital requirements with a tenor ranging between 3 month to 1 year maturity. These are negotiable instruments traded in the secondary market which are also rated by rating agencies.

No.	Terms	Description
24	<b>Bonds</b>	<p>A bond is an organization's promise to repay a sum of money at a certain interest rate and over a certain period of time.</p> <p>A bond is simply a loan in the form of a security with different terminology: The issuer is equivalent to the borrower, the bond holder to the lender, and the coupon to the interest. Bonds enable the issuer to finance long-term investments with external funds.</p>
25	<b>Bond Fund</b>	<p>Debt funds by nature, bond funds like all mutual funds, are investment vehicles. They are meant especially for investors with relatively less appetite for risk and having an intention to earn returns higher than what are possible to earn from other avenues like Fixed Deposits that are considered as safe. So, safety and return both are of equal concern for those investing in Bond Funds. Most bond funds pay income regularly and their NAVs tend to fluctuate less than an equity fund.</p>
26	<b>Bond Funds: Investment Avenues</b>	<p>In order to successfully achieve the goals of the fund, they invest in a multiplicity of debt instruments such as Corporate Papers, papers issued by GOI etc, with different maturities and qualities. In order to balance the liquidity needs of investors who might want to redeem their funds any time, they also have exposure to money market instruments and call papers. Generally, mutual funds invest in bonds issued by different issuers such as government, corporate houses etc.</p>
27	<b>Classification of Bonds</b>	<p>Government Bonds, Corporate Bonds, Municipal Bonds</p>
28	<b>Government Bond</b>	<p>The Government Treasury and its agencies issue these bonds. Treasury bonds are considered the highest quality of all bonds because the credit of the government backs them and so the payment upon maturity is more or less guaranteed. In exchange for this very high margin of credit safety, they have the lowest yields.</p>
29	<b>Corporate Bonds</b>	<p>These are issued by various companies to finance their operations, expansion activities etc. Credit rating agencies such as CRISIL, CARE, ICRA rate these instruments in India on the basis of their degree of safety, which is defined as their ability to pay the amount on maturity. The risk-return trade off is witnessed here as well, for companies with good rating offer less yield.</p>
30	<b>Municipal Bonds</b>	<p>These bonds are issued by governments and municipalities. Considered as reasonably safe, these bonds provide varying returns depending upon their maturities.</p>
31	<b>Features of Bonds</b>	<ul style="list-style-type: none"> <li>● The value of the bond is nothing but the present value of the future cash flows.</li> <li>● For Zero Coupon bonds, the weighted average maturity is same as Duration of the Bond</li> <li>● Weighted average maturity of a coupon bearing bond is less than its tenure.</li> <li>● Higher the weighted average maturity of the bond , higher will the volatility in the price of the bond.</li> <li>● Average maturity indicates the number of years in which the principal will be repaid.</li> </ul>
32	<b>Risk</b>	<p>The uncertainty related to the unfavorable outcome of an event.</p>
33	<b>Types of Risk</b>	<p>Interest Rate Risk, Credit Risk, Delay Risk, Operational Risk, Systematic Risk, Counter Party Risk etc</p>

No.	Terms	Description
34	<b>Credit Risk</b>	Just like shares where the performance of the company has some bearing on the stock prices, credibility of the issuer is of importance in debt instruments. The risk of the issuer not being able to make payments on his liabilities (debt instrument) is termed as default risk or credit risk. This is of special concern to the investor if the fund is investing into junk bonds or lower quality bonds. Bond funds offer professional management and a range of quality ratings to help lower this risk and so investors stand to benefit by the expertise of fund to pick good papers only.
35	<b>Interest Rate Risk</b>	Unlike stock market where an upward movement of market leads to upward movement in stock prices, it is a fall in the market yield that pushes up the prices of debt securities. This happens because there exists an inverse relationship between the yield and the price of a bond. So, if there is an upward movement of interest rates after one has invested in a bond fund, the prices of bonds will go down leading to a corresponding fall in the NAVs of the bond funds.
36	<b>Securitization</b>	Securitization refers to creating marketable securities out of future revenue streams, or simply, raising money by selling cash flows.
37	<b>Pass Through Certificate (PTC)</b>	When mortgages are pooled together and undivided interest in the pool is sold, pass-through securities are created. The term 'undivided' in this context means that each holder of the security has a proportionate interest in each cash flow generated in the pool. The pass-through securities promise that the cash flow from the underlying mortgages would be passed through to the holders of the securities in the form of monthly payments of interest and principal
38	<b>Benefits of PTCs</b>	<ul style="list-style-type: none"> <li>● From the perspective of the company that securitizes its cash flows, the major benefits are in terms of getting immediate cash and passing the risk to the investors.</li> <li>● For finance companies, securitization would take the loan assets off the balance sheet, thereby relieving pressures of capital adequacy.</li> <li>● Flexibility- A pool of receivables could be split into different `strips' and sold to different types of investors. For example, a money market mutual fund might be interested in a short-term paper (pass through certificate), whereas a pension fund might want to invest in a long-term paper. The SPV can have something to offer to both.</li> <li>● Typically, yields in asset-backed securities (car loans, lease rentals etc) are higher than that of other securities of the same rating (Crisil Position Paper on Securitization).</li> <li>● The papers are also considered to be relatively safer. There has been few instances of default or downgrade of rating despite the fact that some of the originators have been downgraded".</li> </ul>

No.	Terms	Description		
39	Difference between PTCs and Bonds	<b>Points of Differentiation</b>	<b>Bonds</b>	<b>PTCs</b>
		Type	Interest bearing debt instrument.	Not direct debt instruments; instead derive their value from other debt instruments.
		Structure	A debt security issued by a company (called the Issuer), which offers to pay interest in lieu of the money borrowed for a certain period. In essence it represents a loan taken by the issuer who pays an agreed rate of interest during the lifetime of the instrument and repays the principal normally, unless otherwise agreed, on maturity.	When mortgages are pooled together and undivided interest in the pool is sold, pass-through securities are created. The pass-through securities promise that the cash flow from the underlying mortgages would be passed through to the holders of the securities in the form of monthly payments of interest and principal.
		Yield	-	Comparatively Higher
		Duration	These are long-term debt instruments issued by private sector companies. These are issued in denomination as low as Rs. 1000 and have maturity ranging between one and ten years.	A pool of receivables could be split into different 'strips' and sold to different types of investors. For example, a money market mutual fund might be interested in a short-term paper (pass through certificate), whereas a pension fund might want to invest in a long-term paper. The SPV can have something to offer to both.
		<p><b>Disclaimer:</b> The Glossary is intended solely for information purpose &amp; does not constitute any opinion or guidelines or recommendation on any course of action to be followed by the reader. Readers are advised to seek independent professional advice and arrive at an informed investment decision before making any investments. The information contained herein has been prepared on the basis of publicly available information, internally developed data and other sources believed to be reliable. None of The Sponsor, The Investment Manager, The Trustee, their respective directors, employees, affiliates or representatives assume any responsibility for, or warrant the accuracy, completeness, adequacy and reliability of such information. Whilst no action has been solicited based upon the information provided herein, due care has been taken to ensure that the facts are accurate and opinions given fair and reasonable. This information is not intended to be an offer or solicitation for the purchase or sale of any financial product or instrument. Recipients of this information should rely on information/data arising out of their own investigations. Readers are advised to seek independent professional advice and arrive at an informed investment decision before making any investments. None of The Sponsor, The Investment Manager, The Trustee, their respective directors, employees, affiliates or representatives shall be liable for any direct, indirect, special, incidental, consequential, punitive or exemplary damages, including lost profits arising in any way from the information contained in this material.</p>		
		Source: BSE Publications, Investopedia.com, investorglossary.com, finance-glossary.com		