May 22, 2011
Chief General Manager
Reserve Bank of India
Internal Debt Management Department
Central Office Building, 23rd floor
Fort, Mumbai 400001

Dear Sir:

On behalf of the Securities Industry and Financial Markets Association (SIFMA), the Asia Securities Industry & Financial Markets Association (ASIFMA), and our member companies, we present the following comments on the Reserve Bank of India's *Proposed Guidelines on Authorization of Primary Dealers ("**PDs**") in India*. We appreciate the opportunity to comment on the Guidelines and share the global banking industry's perspective.

As of April 25, 2011, there were eight standalone PDs and 13 bank PDs operating in India. We understand these PDs play an active role in the Government securities market by underwriting and bidding for fresh issuances and acting as market makers for these securities. We appreciate and are encouraged by PDs continued work with the RBI to ensure that credit is available to the productive sectors of the economy, institutions are established to assist with building the country's financial infrastructure, and access to affordable financial services is expanded.

It is our hope that the following comments will serve to inform and support continued deliberation of this critical policy issue.

Sincerely,

Kenneth E. Bentsen, Jr.
EVP, Public Policy and Advocacy
SIFMA

Nicholas de Boursac
CEO & Managing Director
ASIFMA

1. BACKGROUND

1.1 The system of PDs in the Government Securities ("**G-Sec**") market was introduced in 1995 to strengthen the infrastructure in the G-Sec market, improve the secondary market trading system, which would contribute to price discovery, enhance liquidity and turnover, and encourage voluntary holding of G-Sec amongst a wider investor base, and make PDs an effective conduit for conducting open market operations ("**OMO**"). The current guidelines to authorize PDs in the Indian G-Sec market were prescribed in 1995 when the PD system was introduced in India.

1.2 The Reserve Bank of India ("**RBI**") has now issued a set of Proposed Guidelines on the Authorization of Primary Dealers in India (published on its website on May 4, 2011) (the "**Proposed Guidelines**") and has invited banks, nonbanking financial institutions, all stakeholders and the public at large to comment on the Guidelines.

1.3 We understand the purpose of the guidelines is to make the PD authorization policy more transparent and ensure that new PDs have sound capital, adequate experience and expertise in the G-Sec market, and prudent risk-management measures to enable them to meet their roles and obligations in the Government debt market in an effective manner.

1.4 SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association ("**GFMA**").

1.5 ASIFMA is an independent association whose mission is to promote the development of liquid, efficient and transparent capital markets in Asia and facilitate their orderly integration into the global financial system. Association priorities are driven by the active participation of over 40 member companies, including global and regional banks, securities dealers, brokers, asset managers, credit rating agencies, law firms, trading and analytic platforms, and clearance and settlement providers involved in Asian capital markets. ASIFMA is located in Hong Kong and is the Asian regional member of GFMA.

1.6 We appreciate that the RBI has invited public comments on the Proposed Guidelines and take this opportunity to make recommendations on some of the key policies that RBI has set out for the authorization of primary dealers in India.

1.7 The comments in this submission represent the general collective views of SIFMA and ASIFMA's member companies, rather than the response of any individual member. Nothing in this industry submission is intended to negate or substitute for more detailed, case-specific consultations by individual members or other industry associations.

2. Submission

2.1 Two-year time period for compliance with the minimum turnover requirement

2.1.1 Issue of Concern

As described in **Paragraph 17** of the Proposed Guidelines, existing PDs would be given a two-year time period to comply with the minimum turnover requirement of 15 percent of their total turnover in the G-Sec business during the preceding financial year, to be achieved on behalf of mid-segment (Provident Funds, Urban Cooperative banks, Regional Rural banks, Trusts etc.) and retail (individual) investors.

2.1.2 Comments

Though we understand that PDs are committed to expanding the Government bond market in the retail segment, we believe that PDs may be constrained in dealing with a significant number of players in the mid-segment because of the following factors:

- The Know Your Customers ("**KYC**") norms would be restrictive in the case of Urban Cooperative banks, Regional Rural banks, and Trusts, etc., due to the presence of a high number of politically exposed people on the boards of these entities.

- The financial health of the Urban Cooperative banks and Regional Rural banks may not be financially stable enough for PDs to take exposure on them.

- As standalone PDs, we do not currently provide custodial services. Because of this, it would be very difficult to open a Constituent Subsidiary General Ledger ("**CSGL**") account and hold or trade securities on behalf of these clients.

- Additionally, PDs would not have as an extensive reach as banks have in the case of retail customers.

- We respectfully disagree with the minimum turnover requirement of 15 percent of the total turnover in the G-Sec business during the preceding financial year. Though at this time we are unable to provide specific data on the topic, our general estimates are that the existing market volume in this segment is less than 1 percent of the total volume.

- The current percentage of total retail participation is less than 1 percent of the total market turnover, mainly because there are currently no incentives for retail investors to invest in Government bonds. Individual investors are more likely to invest in other quasi- sovereign instruments, such as Post bank savings or National Stock Exchange ("**NSE**") certificates, which offer better tax adjusted returns.

Additionally, we believe more clarity is required to better determine what is counted toward the "turnover" requirement outlined in **Paragraph 17**.

2.1.3 Recommendation

Instead of mandating a minimum turnover requirement of 15 percent, the RBI should develop an incentive-based program aimed at increasing the depth of Government securities in the mid- and retail segment. Our recommendations include:

- In the current electronic market Negotiated Dealing System Order Matching ("**NDS-OM**") system, which accounts for more than 90 percent of the total market volume, access is limited to wholesale participants and the tradable lot size is restricted to INR 50 mio. The RBI should reduce the minimum lot size to INR 1 mio which would help mid- and retail market participants to get a better price and may also lead to an increase in the overall volume of the G-Sec market.

- The creation of an internet-based trading platform, which can be accessed by the mid- or retail market segment, would help to expand the reach of the market. Primary dealers could make markets on the platform by providing two-way quotes on securities.

- Currently, most retail products marketing, such as Mutual Fund units and Post Office savings schemes, which have a similar credit risk, offer a commission structure for the agents. We suggest a similar commission structure for PDs to encourage mid- and retail market investors to participate in Government bond primary auctions.

2.2 Exit/Termination Procedures

2.2.1 Issue of Concern

Item **iii**) in **Paragraph 19** allows the RBI to suspend or terminate a PD, as it may deem fit, under the following circumstance: repeatedly providing bids and offers in the primary and/or secondary market that are not "reasonably competitive."

2.2.2 Comments

The term "reasonably competitive" is too broad and requires a more precise definition.

Recommendation

2.2.3 We respectfully ask for more clarity on the term "reasonably competitive" to better understand the scope of the RBI's ability to suspend or terminate a PD.

For inquiries or additional information, please contact:

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