ETHICAL CHALLENGES IN INDIAN FINANCIAL MARKET

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Abstract : Ethics in finance consists of the moral norms that apply to financial activity broadly conceived. That finance be conducted according to moral norms is of great importance, not only because of the crucial role that financial activity plays in the personal, economic, political, and social realms but also because of the opportunities for large financial gains that may tempt people to act unethically. Many of the ethical norms in finance are embodied in laws and government regulation and enforced by the courts and regulatory bodies. This study has been undertaken to analyse the ethical challenges faced by Indian financial market, the major corporate scams exposed so far and understanding the role of ethics in avoiding these scams. The success of financial market and services corporation is highly correlated with customer orientation and satisfaction. Unethical marketing practices may lead to create a negative attitude of the customer towards financial service and the same may result in the less channelization of funds which is not good for the health of any financial system.

Keywords– Financial market,Ethics

INTRODUCTION

Finance is considered as the lifeblood of business. Finance is concerned broadly with the generation, allocation, and management of monetary resources for any purpose. It includes personal finance, whereby individuals save, invest, and borrow money to conduct their lives; corporate finance, whereby business organizations raise capital, mainly through the issue of stocks and bonds, and deploy it to engage in economic production; and public finance, whereby governments raise revenue by means of taxation, fees, and borrowing and spend it to provide services for their citizens. This financial activity is facilitated by financial markets, in which money and financial instruments are traded, and by financial intermediaries, such as banks, exchanges, and other financial services providers, which facilitate financial transactions. Ethics in finance consists of the moral norms that apply to financial activity broadly conceived. That finance be conducted according to moral norms is of great importance, not only because of the crucial role that financial activity plays in the personal, economic, political, and social realms but also because of the opportunities for large financial gains that may tempt people to act unethically. Many of the ethical norms in finance are embodied in laws and government regulation and enforced by the courts and regulatory bodies. Ethics plays a vital role, in addition to laws and regulations, first, by guiding the formation of laws and regulations and, second, by guiding conduct in areas not governed by laws and regulations. In general, moral norms reflect the conduct in financial activity that follows from fundamental ethical principles.

Objectives of paper:

- To analyze the ethical challenges faced by Indian financial market
- To analyze the major corporate scams exposed so far and understanding the role of ethics in avoiding these scams.

Research Methodology

The study is based on secondary data. The data has been collected and compiled from various books, journals and websites.

Financial market and Ethics

Financial market refers to a mechanism that allows people to trade financial securities such as stocks, bonds or commodities like precious metals or agricultural goods and other items of values at low transaction cost and at prices that reflect the efficient market hypothesis.

A Framework for Finance Ethics Most financial activity takes the form of financial contracting, in which two parties come to some mutual agreement. For example, bank loans and stock trades are each kinds of contracts. Because so much financial activity consists of contracting, the ethical norms that apply in finance can be grouped under two main heads:

(1) fairness in making contracts and the (2) observance of contractual obligations. Virtually the whole of ethics in finance can be reduced to two simple rules:

(1) “Be fair (in making contracts)!” and (2) “Keep your promises (made in contracts)!” Although the ethical issues that arise in finance are numerous, they, too, can be grouped under a few main heads. These heads are as follows: financial markets, financial services, and financial management.

The main ethical concern in financial markets, such as stock markets, is that they be fair, especially in cases of asymmetry, which occur when parties have unequal information or power. Ethical issues in the financial services industry and in the financial management of corporations mainly involve agents, who have an obligation to act in the interests of other parties, called principals, and fiduciaries, who have a fiduciary duty to act in the interest of beneficiaries. When agents and fiduciaries have a personal interest that interferes with their ability to serve others, they are said to have a conflict of interest. In financial markets, money and financial instruments, such as stocks, bonds, futures, options, and derivatives, are issued or traded. Generally, this activity is conducted in organized markets or exchanges, such as stock or bond markets or commodity exchanges. However, many financial transactions, including the purchase of financial products, such as mutual funds or insurance policies, and private exchanges between two parties can be viewed as taking place in a market. Market activity of any kind may be criticized as unfair. Unfairness in financial markets is commonly ascribed to unfair trading practices (most notably, fraud and manipulation), the conditions under which a trade is made (which are often described as an unlevel playing field), and difficulties in the contracting process (i.e., in forming, interpreting, and enforcing contracts).

Fairness or unfairness in financial markets may be further classified as substantive or procedural. A stock trade, for example, is fair in substance when the price reflects the actual value of the shares. It is fair in procedure when the trading parties have sufficient opportunity to accurately determine the value of the shares. Thus, “blue sky laws,” which require expert evaluation of securities offered for sale, aim at substantive fairness, whereas regulations that merely require disclosure of relevant information aim at procedural fairness. Trading Practices Fraud in a financial transaction is committed when one party knowingly makes a material misstatement or omission that the other party reasonably relies on to his or her detriment. Fraud thus has five elements: (1) a false statement about, or the concealment of, some fact; (2) the significance or materiality of this fact; (3) knowledge of the falsity of the statement, which indicates an intent to deceive; (4) reliance by the victim of the fraud on the information provided; and (5) some harm to the victim. Fraud is an unfair trading practice because the perpetrator uses dishonest means to induce the victim to make a trade that he or she would not make otherwise. Whereas fraud creates a false belief by means of a statement or an omission, manipulation deceives others by creating a false impression. In a so-called pump and dump scheme, for example, a trader buys a thinly traded stock to drive up the price (pumps) and then sells at the artificially created high price (dumps). Nothing false need be said in such a scheme, but the trading activity creates a false impression about prices that induces others to trade. Some large institutional investors have been accused of manipulating markets by creating volatility that they can exploit with sophisticated trading strategies. Fair Conditions A fair market, like a fair sports contest, requires a level playing field in which no one has an unfair advantage. A financial market may be unfair or unlevel either because of inequalities in information, bargaining power, resources, or processing ability or because of special vulnerabilities. Unequal information, or information asymmetry, results when two parties either do not possess the same information or do not have the same access to information. Neither kind of information asymmetry is necessarily unfair; market participants inevitably differ in their possession of and access to information. However, it is wrong under some conditions to take advantage of another's ignorance or weakness. Thus, the law requires that issuers of securities (e.g., stocks and bonds) or financial products (e.g., a mutual fund) provide a prospectus that offers sufficient information for buyers to make informed decisions. Insider trading—which is trading by insiders of a company on the basis of material, non-public information—is illegal, in part, because the parties on the other side of the transaction, being outsiders, cannot obtain the same information. The insider is thus taking unfair advantage of a privileged position. In general, it is unfair to take advantage of different conditions when doing so violates some right or obligation. Thus, a prospectus is required for the issuance of securities because the buyers have a right to make an informed decision. In cases of insider trading, the insider is usually violating a fiduciary duty to the corporation not to use confidential information for personal gain. Laws that impose a "cooling-off" period during which a buyer can cancel a large purchase or loan may be justified on the ground that it is wrong to take advantage of people's impulsiveness or inexperience. In other words, people have a right not to be taken advantage of in certain ways.

Major Financial Scams in India:

Security scams and financial scandals have led to the manipulation of large amount of money, bloating stock markets and Sensex.

1)Harshad Mehta Scam: It was in 1992 the estimated size of the scam was 4000crores in that scam they used money from banks to make personal gains via investment in shares.

2) CR Bhansali Scam : It was in 1996 the estimated size of that scam was1200 crores in that scam they raised public money through FDs, MFs and debentures via non-existent firms and invested them in stocks for personal gains.

3) Ketan Parekh Scam: It was in 2001 the estimated size was 800 crores through circular trading in selected stocks via borrowed money from banks to manipulate share prices. Ketan Parekh, a Mumbai based stock broker and a qualified chartered accountant had large borrowings from Global Trust Bank during its Merger with United Trust of India Bank. He got a loan of about Rs.250 Crores from Global Trust Bank's Chairman Mr. Ramesh Gelli. The prices of the selective shares constantly increased due to rigging .The investors who bought the share at higher prices thought that the market prices were genuine. Soon after the discovery of the scam of 1999-2000, the price of the stocks came down to the fraction of value at which they were purchased. The investors lost heavily. Even the banks faced a tremendous loss. The amount involved in this scam was estimated to be around 1500 crores

4) Satyam Scam it was discovered in 2009 the estimated Size was : Rs 14,162 crore The top management of the software company cooked up accounts to show inflated sales, profits and margins from 2003 to 2008. Coming on the back of global recession, this incident busts the Indian Outsourcing Industry and the stock market.

5) Sahara Housing Bonds scam It was in 2010 estimated Size was Rs 24,029 crore they were issued bonds to 29.6 million investors without following SEBI regulations and investor protection measures mentioned therein.

6) Speak Asia scam it was in 2012 the estimated size was Rs 2200 crore in this scam Investors were asked to subscribe to an e-magazine for a certain sum, after which they became eligible to answer surveys and got paid for each survey.

7) Saradha Scam it was discovered in 2013 estimated size was Rs.10000 core through this scam multiple investment schemes collected money from nearly 1.4 million investors in West Bengal and Odisha.

8) NSEL Scam it was discovered in 2013 the estimated Size was Rs 5,600 crore in this Investors were wooed by offering fixed returns on paired contracts with agricultural and industrial commodities as underlying. the stocks were missing and money was allegedly siphoned by so-called borrowers.

The above mentioned scams are enough to shatter the confidence of an average investor who puts his hard earned money in a wish to earn something more. Although the finance industry is growing at a multiplier rate with all efforts being directed towards investors security, but the public perception of most financial firms as interested in making money at the expense of all other considerations seems to be unchanging. The financial services sector has an increasingly difficult task balancing the demands of a lengthening list of 'stakeholders' - shareholders, the community, investors and pressure groups and demands of the regulator as well.

A well-functioning market economy requires the existence of and compliance with rules of conduct, and of a series of conditions that must be met for markets and economic institutions to ensure efficient outcomes (such as compliance with contractual obligations, no recourse to corruption, and the non-misuse of information in one's possession). In such a scenario, the benefit to the individual, the cost-effectiveness of adhering to social ethics, stems from the increased collective welfare which this behaviour ensures if it is adopted and respected by all members of the "group" (one society, one economy). However, an issue of collective action arises: only if "everyone" adopts these behaviours will there be a collective benefit; for individuals, the cost can be high; the benefits flowing from non-compliance can be substantial.

It can be clearly observed that one of the major reasons of ethical lapses in the financial sector is greed of mankind. This greed becomes an accumulation fever. If you accumulate for the sake of accumulation, it becomes the end by itself and if accumulation becomes the end, there is no place to stop. So the moral of the story is that we should never allow the self-interest turn into greed and selfishness.

Conclusion

The scams which go into crores of rupees are just a symptom of a problem that runs deep into the very subject of ethics. This poses a biggest challenge to the financial industry. An individual is not born ethical or unethical. It is his surrounding environment that has a larger bearing on a human's ethics. It directly points out to the overall process of growth and development through which a human being undergoes in his lifetime. Financial market and service sector is the backbone of any economy. Without a healthy financial services sector a country cannot take its step ahead for sustainable development. The success of financial market and services corporation is highly correlated with customer orientation and satisfaction. Unethical marketing practices may lead to create a negative attitude of the customer towards financial service and the same may result in the less channelization of funds which is not good for the health of any financial system.

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