Money Market Instruments
Money market instruments are generally characterized by a high degree of safety and are most commonly issued in units of $1 million or more. Maturities range from one day to one year; the most common are three months or less. Active secondary markets for most of the instruments allow them to be sold prior to maturity. Unlike organized securities or commodities exchanges, the money market has no specific location. Available from financial institutions, money markets give the smaller investor the opportunity to get in on treasury securities. The institution buys a variety of treasury securities with the money you invest. The rate of return changes daily, and services such as check writing may be offered. The major participants in the money market are commercial banks, governments, corporations, government-sponsored enterprises, money market mutual funds, futures market exchanges, brokers and dealers. Some of the money market instruments are:

a. Treasury Bills
These are issued by the Reserve Bank usually a period of 91 days. The Reserve Bank uses these bills to take money out of the market. This will reduce a banks ability to lend to its clients leading to a contraction of the money supply. The bill consists of an obligation to pay the bearer the face value of the bill upon a given date. A bank buying such a bill will not pay face value for it but would instead buy it at a discount. The bill is tradable so the purchaser does not have to hold it until the due date. If interest rates decrease during the term of the bill, the holder can sell the bill at a profit before the due date.

b. Bankers Acceptance
Although BA’s, as they are known, have their origin in trade bills issued by merchants, today they are an important money market instrument. A banker’s acceptance is simply a bill of exchange drawn by a person and accepted by a bank. The person drawing the bill must have a good credit rating otherwise the BA will not be tradable. The drawer promises to make payment of the face value upon a given future date. The most common term for these instruments is 90 days. They can vary from 30 days to 180 days. The BA has the advantage of locking the borrower in to a fixed rate over the term of the bill. This can be important if a rise in short-term rates is expected.

c. Negotiable Certificates of Deposit (NCD)
NCD’s are like fixed deposits except they are bearer documents. They offer a market related rate of interest and are completely liquid because they can be negotiated during the term of the deposit. Most NCD’s have a term of less than one year. They usually offer a rate of return slightly higher than banker’s acceptances which makes them extremely popular instruments.

d. Repo/ Reverse Repo
A repo agreement is the sale of a security with a commitment to repurchase the same security as a specified price and on specified date while a reverse repo is purchase of security with a commitment to sell at predetermined price and date. A repo transaction for party would mean reverse repo for the second party. In lieu of the loan, the borrower pays a contracted rate to the lender, which is called the repo rate. As against the call money market where the lending is totally unsecured, the lending in the repo is backed by a simultaneous transfer of securities. The main players in this market are all institutional players like banks, primary dealers like PNB Gilts Limited, financial institutions, mutual funds, insurance companies etc. allowed to operate a SGL with the Reserve Bank of India.

Further RBI also operates daily repo/ reverse repo auctions to provide a benchmark rates in the markets as well as managing in the liquidity in the system. RBI sucks or injects liquidity in the banking system by daily repo/ reverse operations.

e. Certificates of Deposit (CD’s)
Money in a CD is tied up from few months to six years or more depending on the terms of the specific CD you buy. A notice of withdrawal is required and a penalty imposed if you withdraw money before the CD matures. Interest earned is higher than paid on insured savings accounts. The longer you tie up money in a CD, the higher the interest rate earned. Interest is paid either at time of purchase or at maturity, depending on the policy of the financial institution. In most cases, the more money you invest, the higher the rate of interest earned. All earnings are subject to income tax. CD’s are available from banks, savings and loans and credit unions. No purchase fees are charged.

Tax-Exempt Bonds
Often referred to as municipal bonds, tax-exempt bonds represent state and local government debt. A City, town, or a village and also states, territories, and housing authorities, port authorities, and local government agencies may issue these bonds. Interest earned is exempt from income taxes and from state and local income taxes if bonds issued are from your state or city. Interest rates are determined by the general level of interest rates and by the credit rating of the issuer. The seller of these bonds has tables showing you what the taxexempt yields of these bonds are equivalent to in taxable yield for your tax bracket. As little as $1,000 may be invested in these bonds, available from a broker or a financial institution.

Type 3 investments include corporate bonds and corporate stocks. Higher investment risk and lower purchasing power risk are represented by these investment alternatives.