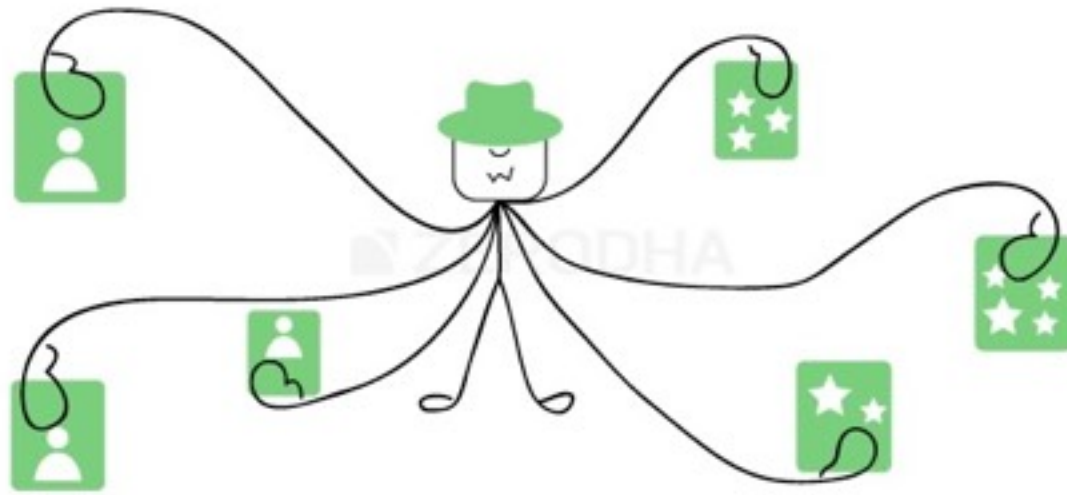


Financial Intermediaries



3.1 - Overview

From the time you access the market – let's just say, to buy a stock till the time the stocks comes and hits your DEMAT account, a bunch of corporate entities are actively involved in making this work for you. These entities play their role quietly behind the scene, always complying with the rules laid out by SEBI and ensure an effortless and smooth experience for your transactions in the stock market. These entities are generally referred to as the Financial Intermediaries.

Together, these financial intermediaries, interdependent of one another, create an ecosystem in which the financial markets exists. This chapter will help you get an overview of who these financial intermediaries are and the services they offer.



3.2 - The Stock Broker

The stock broker is probably one of the most important financial intermediaries that you need to know. A stock broker is a corporate entity, registered as a trading member with the stock exchange and holds a stock broking license. They operate under the guidelines prescribed by SEBI.

A stock broker is your gateway to stock exchanges. To begin with, you need to open something called as a 'Trading Account' with a broker who meets your requirement. Your requirement could be as simple as the proximity between the broker's office and your house. At the same time it can be as complicated as identifying a broker who can provide you a single platform using which you can transact across multiple exchanges across the world. At a later point we will discuss what these requirements could be and how to choose the right broker.

A trading account lets you carry financial transactions in the market. A trading account is an account with the broker which lets the investor to buy/sell securities.

So assuming you have a trading account - whenever you want to transact in the markets you need to interact with your broker. There are few standard ways through which you can interact with your broker.

1. You can go to the broker's office and meet the dealer in the broker's office and tell him what you wish to do. A dealer is an executive at the stock broker's office who carries out these transactions on your behalf.
2. You can make a telephone call to your broker, identify yourself with your client code (account code) and place an order for your transaction. The dealer at the other end will execute the order for you and confirm the status of the same while you are still on the call.
3. Do it yourself – this is perhaps the most popular way of transacting in the markets. The broker gives you access to the market through software called 'Trading Terminal'. After you login in to the trading terminal, you can view live price quotes from the market, and can also place orders yourself.

The basic services provided by the brokers includes..

1. Give you access to markets and letting you transact
2. Give you margins for trading – We will discuss this point at a later stage
3. Provide support – Dealing support if you have to call and trade. Software support if you have issues with the trading terminal

4. Issue contract notes for the transactions – A contract note is a written confirmation detailing the transactions you have carried out during the day
5. Facilitate the fund transfer between your trading and bank account
6. Provide you with a back office login – using which you can see the summary of your account
7. The broker charges a fee for the services that he provides called the ‘brokerage charge’ or just brokerage. The brokerage rates vary, and its up to you to find a broker who strikes a balance between the fee he collects versus the services he provides.



3.3 - Depository and Depository Participants

When you buy a property the only way to identify and claim that you actually own the property is by producing the property papers. Hence it becomes extremely important to store the property papers in a safe and secure place.

Likewise when you buy a share (a share represents a part ownership in a company) the only way to claim your ownership is by producing your share certificate. A share certificate is nothing but a piece of document entitling you as the owner of the shares in a company.

Before 1996 the share certificate was in paper format however post 1996, the share certificates were converted to digital form. The process of converting paper format share certificate into digital format share certificate is called “Dematerialization” often abbreviated as DEMAT.

The share certificate in DEMAT format has to be stored digitally. The storage place for the digital share certificate is the ‘DEMAT Account’. A Depository is a financial intermediary which offers the service of Demat account. A DEMAT account in your name will have all the shares in electronic format you have bought. Think of DEMAT account as a digital vault for your shares.

As you may have guessed, the trading account from your broker and the DEMAT account from the Depository are interlinked.

So for example if your idea is to buy Infosys shares then all you need to do is open your trading account, look for the prices of Infosys and buy it. Once the transaction is complete, the role of your trading account is done. After you buy, the shares of Infosys will automatically come and sit in your DEMAT account.

Likewise when you wish to sell Infosys shares, all you have to do is open your trading account and sell the stock. This takes care of the transaction part...however in the backend, the shares which

are sitting in your DEMAT account will get debited, and the shares move out of your DEMAT account.

At present there are only two depositories offering you DEMAT account services. They are The National Securities Depository Limited (NSDL) and Central Depository Services (India) Limited. There is virtually no difference between the two and both of them operate under strict SEBI regulations.

Just like the way you cannot walk into National Stock Exchange's office to open a trading account, you cannot walk into a Depository to open a DEMAT account. To open a DEMAT account you need to liaison with a Depository Participant (DP). A DP helps you set up your DEMAT account with a Depository. A DP acts as an agent to the Depository. Needless to say, even the DP is governed by the regulations laid out by the SEBI.



3.4 - Banks

Banks play a very straight forward role in the market ecosystem. They help in facilitating the fund transfer from your bank account to your trading account. You may be interested to note that for a given trading account only one bank account can be interlinked. You cannot transfer money from a bank account that is not in your name.

If you have multiple bank accounts, you need to specify which particular bank account that will be linked to your trading account. Of course you can remove the bank account and link it with another bank account of yours, but that requires some amount of paper work. However, for the money to come in and go out of your trading account, it has to happen only via the bank account that has been specified and linked.

Also, at this stage, you must have realized that the three financial intermediaries operate via three different accounts - trading account, DEMAT account and Bank account. All the three accounts operate electronically and are interlinked giving you a very seamless experience.



3.5 NSCCL and ICCL

NSCCL – National Security Clearing Corporation Ltd and Indian Clearing Corporation are wholly owned subsidiaries of National Stock Exchange and Bombay Stock Exchange respectively.

The job of the clearing corporation is to ensure guaranteed settlement of your trades/ transactions. For example if you were to buy 1 share of Biocon at Rs.446 per share there must be someone who has sold that 1 share to you at Rs.446 . For this transaction, you will be debited

Rs.446 from your trading account and someone must be credited that Rs.446 toward the sale of Biocon. In a typical transaction like this the clearing corporation's role is to ensure the following:

- a) Identify the buyer and seller and match the debit and credit process
- b) Ensure no defaults – The clearing corporation also ensures there are no defaults by either party. For instance the seller after selling the shares should not be in a position to back out thereby defaulting in his transaction.

For all practical purposes, its ok not to know much about NSCCL or ICCL simply because, you as a trader or investor would not be interacting with these agencies directly. You just need to be aware that there are certain professional institutions which are heavily regulated and they work towards smooth settlement, and efficient clearing activity.

Key takeaways from this chapter

1. The market ecosystem is built by a cluster of financial intermediaries, each offering services that are unique to the functioning of markets
2. A stock broker is your access to markets, so make sure you choose a broker that matches your requirements, and services well.
3. A stock broker provides you a trading account which is used for all market related transactions (buying and selling of financial instruments like shares)
4. A Depository Participant (DP) is a corporate entity that holds the shares in electronic form against your name in your account. Your account with the DP is called the 'DEMAT' account
5. There are only two depositories in India – NSDL and CDSL
6. To open a DEMAT account with one of the depositories you need to liaison with a Depository Participant (DP). A DP functions as an agent to the Depository
7. A clearing corporation works towards clearing and settling of trades executed by you.

